

1991

U.S. West Communications, Inc. v. Public Service
Commission of Utah; Brian T. Stewart, Chairman,
James M. Byrne, Commissioner, Stephen F.
Meacham, Commissioner : Brief of Appellant

Utah Supreme Court

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UTAH SUPREME COURT
BRIEF
CKET NO. 910408

IN THE SUPREME COURT

STATE OF UTAH

U S WEST Communications, Inc.

Petitioner,

Public Service Commission Of Utah;
Brian T. Stewart, Chairman, James
M. Byrne, Commissioner, Stephen F.
Meacham, Commissioner,

Respondents.

Case No. 910408

Argument Priority No. 10

BRIEF OF APPELLANT U S WEST COMMUNICATIONS, INC.

**ON PETITION FOR REVIEW FROM THE
UTAH PUBLIC SERVICE COMMISSION**

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STATEMENT OF JURISDICTION

The Utah Supreme Court has jurisdiction over this appeal under Article VIII, Section 3 of the Utah Constitution, Utah Code Ann. §§ 63-46b-16(1) and 78-2-2(3)(e)(i), and Rule 14, Utah Rules of Appellate Procedure (URAP).

STATEMENT OF THE ISSUES

1. Did the Commission, in concluding that the Stipulation precludes the Commission from considering the normalization adjustments proposed by Appellant U S WEST Communications (USWC),¹ erroneously interpret and apply the terms of the Stipulation?

Standard of Review: Stipulations are interpreted under the general principles of contract law. Kinsman v. Kinsman, 748 P.2d 210, 212 (Utah App. 1988). The interpretation of a contract is a general question of law to be reviewed under the correction-of-error standard. Savage Industries v. State Tax Comm'n. 811 P.2d 664, 668 (Utah 1991); Morton International v. Auditing Division, 814 P.2d 581, 585 (Utah 1991).

2. Was the Public Service Commission's finding that service in the 41 central offices served by electromechanical central office switches is inadequate under present day standards based on sufficient subsidiary findings?

Standard of Review: The legal sufficiency of findings of fact is a question of law for a reviewing court. Mountain States Legal Foundation v. Public Serv.

¹ For purposes of this Brief, Appellant U S WEST Communications, Inc. will be referred to as "USWC."

Comm'n, 636 P.2d 1047, 1051-52 (Utah 1981); Milne Truck Lines, Inc. v. Public Serv. Comm'n, 720 P.2d 1373, 1378 (Utah 1986). Thus, the determination of whether the findings are adequate should be reviewed under the correction-of-error standard. Savage Industries, 811 P.2d at 668; Morton International, 814 P.2d at 585.

3. Does the Commission's failure to define the standards under which it found that service in 41 central offices served by electromechanical central office switches to be inadequate render the finding so vague as to be unreviewable?

Standard of Review: The question whether an administrative agency has provided an adequate definition of the standards under which it makes a finding of fact is a general question of law. Mountain States Legal Foundation, 636 P.2d at 1051-52; Milne Truck Lines, 720 P.2d at 1378; Adams v. Board of Review, 821 P.2d 1, 7-8 (Utah App. 1991). Thus, the issue is reviewed under the correction-of-error standard. Savage Industries, 811 P.2d at 668; Morton International, 814 P.2d at 585.

4. Is the Commission's finding that service in 41 central offices served by electromechanical central office switches is inadequate under present day standards based on substantial evidence in the record?

Standard of Review: This issue is to be reviewed under the substantial evidence test, under which it will be sustained if "supported by substantial evidence when viewed in light of the whole record." Utah Code Ann. § 63-46b-16(4)(g).

5. Does the Commission's refusal to either consider or make a finding based on the economic study of the 41 central offices, despite the fact it was timely filed and uncontradicted, constitute prejudicial error to USWC?

Standard of Review: The legal propriety of an administrative agency refusing to consider relevant uncontradicted evidence is a general question of law. See Jones v. California Packing Corp., 244 P.2d 640, 644 (Utah 1952); Cf. Jensen v. Logan City, 88 P.2d 459, 460 (Utah 1939). Thus, the determination of this issue should be made under the correction-of-error standard. Savage Industries, 811 P.2d at 668; Morton International, 814 P.2d at 585.

6. Was the Public Service Commission's finding that the fiber optic backbone and distance learning facilities are inadequate under present day standards based on sufficient subsidiary findings?

Standard of Review: The legal sufficiency of findings of fact is a question of law for a reviewing court. Mountain States Legal Foundation, 636 P.2d at 1051-52; Milne Truck Lines, 720 P.2d at 1378. Thus, the determination of whether there are adequate findings should be reviewed under the correction-of-error standard. Savage Industries, 811 P.2d at 668; Morton International, 814 P.2d at 585.

7. Does the Commission's failure to define the standards under which it found that the fiber optic backbone and distance learning facilities to be inadequate render the finding so vague as to be unreviewable?

Standard of Review: The question whether an administrative agency has provided an adequate definition of the standards under which it makes a finding

of fact is a general question of law. Mountain States Legal Foundation, 636 P.2d at 1051-52; Milne Truck Lines, 720 P.2d at 1378 ; Adams v. Board of Review, 821 P.2d 1, 7-8 (Utah App. 1991). Thus, the issue is reviewed under the correction-of-error standard. Savage Industries, 811 P.2d at 668; Morton International, 814 P.2d at 585.

8. Is the Commission's finding that the fiber optic and distance learning facilities are inadequate under present day standards based on substantial evidence in the record?

Standard of Review: This issue is to be reviewed under the substantial evidence test, under which it will be sustained if "supported by substantial evidence when viewed in light of the whole record." Utah Code Ann. § 63-46b-16(4)(g).

9. Did the Commission violate the due process rights of USWC by ordering the deployment of the fiber optic backbone and the distance learning facilities when no party sought such relief or presented any evidence in support of such an order?

Standard of Review: A determination of whether the constitutional rights of a party have been violated is a general question of law to be reviewed under the correction-of-error standard. Savage Industries, 811 P.2d at 667; Morton International, 814 P.2d at 585.

DETERMINATIVE CONSTITUTIONAL PROVISIONS AND STATUTES

The following constitutional provisions and statutes are relevant and may be determinative of some of the issues raised in this Appeal: U. S. Constitution, Amendments V and XIV; Utah Constitution, Article I, Section 7; Utah Code Ann. §§ 54-4-7 and 63-46b-16(4).

STATEMENT OF THE CASE

The Commission's June 19, 1991 order sets forth a detailed procedural history of this proceeding. (R. 5384-88)² The portions of the Report and Order relevant to this appeal are attached as Addendum A. The following Statement of the Case focuses on the course of the proceedings relevant only to the specific issues in this appeal.

On March 2, 1990, USWC filed an Application with the Commission pursuant to Utah Code Ann. § 54-4-4.1 seeking approval of an incentive regulation plan.³ (R. 3739-60) In the proposed plan, USWC agreed to modernize 41 central

² Also, in a separate appeal of the Commission's Order (Supreme Court Docket No. 910405), the briefs contained lengthy expositions of the procedural history of this case.

³ Incentive regulation plans are often referred to as "earnings sharing" plans. They represent a recent trend in the regulation of telephone utilities. While no two plans are identical, there are two features common to most plans: (1) some form of rate freeze on basic telephone services for the term of the plan (normally 3 to 5 years) (R. 7987, 8000) and (2) some mechanism by which profits above a predetermined level are shared by the utility and ratepayers. (R. 7816, 8307) The underlying theory is that the rate freeze and revenue sharing protect ratepayers while, at the same time, the higher earnings opportunity will create incentives for the utility to be more efficient. (R. 7295-99, 7301-02, 7808-09, 7987-89,

offices in Utah, contingent upon the Commission approving a plan acceptable to USWC.⁴ The Application was assigned Docket No. 90-049-03. On March 28, 1990, the Division of Public Utilities (hereinafter "Division") filed a Petition in Docket No. 90-049-06 seeking an investigation into the reasonableness of the rates and charges of USWC. (R. 4241-60) These dockets were later consolidated for hearing. (R. 3875-82)

In Docket No. 90-049-06, the Division and the Committee of Consumer Services (hereinafter "Committee") requested, pursuant to Utah Code Ann. § 54-7-12(3), that USWC's rates be reduced on an interim basis. The Commission held hearings in May 1990 to consider whether to order a decrease of USWC's rates on an interim basis during the pendency of the rate proceeding. Following those hearings, the Commission, on June 22, 1990, issued an order reducing the rates of USWC on an interim basis by \$10.65 million. (R. 4490-505)

Thereafter, extensive testimony was filed by several parties with regard to (1) the incentive regulation plan (including issues relating to network modernization), (2) rate of return, accounting adjustments and other related

8037-47) These plans also often include such things as service improvement requirements and network upgrades. The USWC plan included network upgrades.

⁴ The Utah statute authorizing earnings sharing plans gives the utility the power to opt out of a plan that is unacceptable to it. Utah Code Ann. § 54-4-4.1(2).

issues,⁵ and (3) rate spread issues.⁶ On October 30, 1990, USWC, the Division and the Committee entered into a Stipulation (hereinafter referred to as the "Stipulation") resolving most revenue requirement issues in the case. (R. 4567-83, Addendum B) The Stipulation was approved by the Commission on January 3, 1991. (R. 4654-56) Hearings on all remaining issues were held in December 1990, and February and March 1991. In April 1991, USWC, the Division and Committee made additional filings relating to disputed issues under the Stipulation. (R. 6032-59, 7167-94, 8321-80)

On June 19, 1991, the Commission issued a 103 page order (excerpts attached as Addendum A). In that order, the Commission, among other things, (1) ordered additional rate reductions of \$19.799 million (R. 5481), (2) rejected incentive regulation plans proposed by USWC and the Division (R. 5477), (3) outlined an incentive regulation plan designed by the Commission (R. 5478-80), (4) ordered USWC (irrespective of its acceptance or rejection of the incentive regulation plan adopted by the Commission) to replace switching equipment in 41 rural central offices by the end of 1996 and to deploy fiber optic technology between

⁵ These are commonly referred to as "revenue requirement" issues. Through the resolution of these issues, the Commission determines the overall change in the utility's revenue requirement. If current revenues exceed the revenue requirement determined by the Commission, an overall rate reduction is ordered. If current revenues are less than the revenue requirement, the Commission orders an overall increase.

⁶ In the "rate spread" portion of the case, the Commission determines which specific rates will change and by what amount to achieve the overall revenue change.

Nephi and St. George by the end of 1996 (R. 5461, 5481), and (5) ordered USWC to work with the Division and educational institutions in Utah to devise a program for extending fiber optic technology to such institutions for purposes of providing educational telecommunications services. (R. 5461-62, 5481)

On June 21, 1992, USWC moved to stay the entire \$19.799 million rate reduction. (R. 5505-19) On July 3, 1991, the Commission denied the motion. (R. 5540-47) On July 19, 1991, USWC filed its Petition for Review, Reconsideration and Rehearing of the June 22, 1990 Interim Order and the June 19, 1991 Order. (R. 5610-62) In its Petition, USWC raised a variety of issues, including those that are the subject of this appeal.⁷ On July 22, 1991, the Commission granted rehearing to the extent of allowing oral argument by the parties. (R. 5663-64) On August 13, 1991, the Commission issued its Order on Review (attached as Addendum C) rejecting all of the claims of USWC that are relevant to this appeal. (R. 5695-707) On August 15, 1991, USWC filed its election not to proceed with the incentive regulation plan adopted by the Commission. (R. 5692-94) On August 22, 1991, USWC filed a Petition asking the Commission to stay those portions of the June 19 order requiring USWC to perform certain network modernization by the end of 1996. (R. 5717-25) On August 30, 1991, the Commission denied the Petition for a Stay. (R. 5745-51)

⁷ USWC claimed that (1) the Commission had erred in its interpretation of the Stipulation and that the error resulted in a rate reduction that exceeded a reasonable amount by \$5.916 million (R. 5614-23), and (2) that the Commission's order regarding network modernization was illegal and unenforceable (R. 5624-41).

On September 11, 1991, USWC filed its Petition for Review with this Court. The case was assigned Docket No. 910408. On September 20, 1991, USWC filed a Motion seeking a stay of \$5.96 million of the \$19.779 million rate decrease. On October 2, 1991, USWC filed a Docketing Statement in which it preserved all the issues raised in this Brief for appeal. Following filings by other parties and oral argument, this Court denied USWC's Motion to Stay on November 8, 1991.

STATEMENT OF FACTS

The following Statement of Facts focuses only on the factual issues relevant to this appeal.

A. The Stipulation. The Petition filed by the Division on March 28, 1990 created what is commonly known as a "show cause" rate proceeding – a general rate case initiated by a party other than the utility seeking an overall reduction in rates. Such a proceeding has all the attributes of a general rate case initiated by a utility – it involves a general inquiry into the overall revenues, expenses and investment of the utility and results in an order requiring an overall reduction or increase in rates. In such a case, there are literally hundreds of potential revenue requirement issues that parties can raise, ranging from the appropriate rate of return to specific accounting adjustments and expense disallowances. To meaningfully determine whether an overall increase or decrease in revenues is appropriate, a test period must be developed, the purpose of which "is to provide revenue, expense, and investment information that reasonably approximates the

circumstances expected during the period rates will be in effect.”⁸ In this show cause proceeding, a 1990 test year was used by the parties and accepted by the Commission, despite the fact that the case was filed in early 1990 and a full year’s financial results were not available. Prior to the filing of testimony on the full range of revenue requirement issues, USWC, the Division, the Committee, and AT&T entered a Stipulation and Joint Motion on Revenue Requirement Issues (“the Stipulation”) on October 30, 1990. (R. 1567-83, Addendum B) The Stipulation is the key document relating to Point I of USWC’s appeal. The Stipulation did not resolve all revenue requirement issues. Specifically excluded from the Stipulation were issues relating to rate of return, capital structure, and depreciation represcription. (R. 4569)⁹ Because the test year was calendar year 1990 and since a full test year’s data was unavailable when the Stipulation was entered, the agreement of the parties on specific issues fell into two categories: (1) as to certain adjustments and disallowances, the parties reached absolute agreements as to their resolution and quantification, which were not subject to later amendment

⁸ In the Matter of the Investigation of the Reasonableness of the Rates and Tariffs of Mountain Fuel Supply, Report and Order at 6 (Utah P.S.C., November 21, 1990).

⁹ The Stipulation included Joint Exhibit 1 (JE-1), which was based on six months of test year financial results. The reason more financial information was not available is that telephone utilities are subject to dual regulation by the FCC and by state commissions. As a consequence, there is an extremely complicated process by which revenues, expenses and investment are separated between the FCC regulated interstate jurisdiction and the state regulated intrastate jurisdiction. The result is that the separation process causes an approximate two-month lag between the end of a particular month and the receipt of earnings information that is usable by a state commission.

based on updated financial results of USWC, and (2) with regard to other issues, the parties agreed that their quantification would change as additional test year financial results became available. (R. 4573-74) The language of the Stipulation specifically contemplated that the actual test year results would be updated and would be subject to adjustments so that the financial results upon which the rate order would be based would meet the Commission's goal of a representative test year for rate setting purposes.

The parties explicitly agreed that the additional test year data would be "annualized and normalized." Paragraph 5 of the Stipulation states: "For illustrative purposes, the parties have calculated JE-1 using six months actual results which have been annualized and normalized and the most recently found rate of return on equity, USWC's current actual capital structure and with no increase in depreciation rates." (emphasis added). Paragraph 5 further stated that the final calculation of the revenue requirement would use "updated results." (R. 4573)

In paragraph 6, the parties agreed that several of the columns in JE-1 "shall be updated monthly with additional actual data." The parties further agreed that, at the time of later hearings, which were then scheduled for December, "the parties will provide the latest updated JE-1 which will present nine months actual results on an annualized and normalized basis consistent with the annualization and normalization of six months actual data in JE-1." *Id.* (emphasis added).

Finally, paragraph 9 describes how the implementation of the final order will take place. It stated that the final order would incorporate changes in revenue requirements resulting from the rate of return decision, the decision regarding depreciation represcription, and "updating JE-1 for at least 11 months actual test year results." (R. 4575)

The key provision in the Stipulation is the agreement that the updated results would be "normalized." Normalization is an accounting term of art in utility regulation that refers to the elimination of abnormal or non-recurring financial accounting events from a test year so that revenues, expenses and investments are properly matched so that the test year will serve its function of being a reasonable proxy for the time in which rates will be in effect.¹⁰ By explicitly agreeing that the updated financial results would be normalized, the parties contemplated (1) that the financial results for the last six months of 1990 would be subject to appropriate normalizing adjustments, and (2) that the parties had the right, prior to the finalization of JE-1, to present such adjustments to the Commission for resolution.

During the remainder of 1990 and in early 1991, as additional monthly financial results were received, USWC provided them to the Commission, Division and Committee. As early as December 1990, in the Commission hearing to determine whether to approve the Stipulation, Mr. Henningsen of the Division testified that USWC had noted a problem with the tax numbers reflected in the

¹⁰ For a more detailed discussion of the meaning of "normalization" in the context of utility ratemaking, see Section I.A. infra.

actual financial results, which was being investigated. (R. 464-65). In early 1991, when the November and December 1990 separated financial results became available, it became clear to USWC that the actual results did not produce an appropriately normalized test year because of several 1990 accounting entries that related to prior years. (R. 8323) USWC, therefore, informed the Division that it was investigating the matter, noting that, prior to finalizing JE-1 under the Stipulation, it would be necessary to identify and consider what adjustments should be made. (R. 7160) On April 5, the Division filed an updated JE-1, which identified the normalization adjustments the Company proposed to make to the test year under the terms of the Stipulation. (R. 7160-66, esp. 7165) On April 9, the Committee propounded a detailed set of data requests regarding the adjustments. (R. 8324) Three days later, those data requests were responded to in detail by USWC. Id. Thereafter, the parties filed a series of position statements outlining their positions on two issues: (1) whether the adjustments could be proposed under the terms of the Stipulation, and (2) the validity of the specific adjustments. (R. 6032-59, 7167-94, 8321-80) Oral argument on the position statements was held on May 15. (R. 3496-3588) Pursuant to USWC's Motion, which was supported by the Committee (R. 5341), the position statements were received as evidence without objection.¹¹ The record, therefore, contains detailed evidence relating to

¹¹ In its Notice of Hearing establishing oral argument, the Commission noted that it had "determined to receive the position statements as evidence for purposes of its decision in this proceeding." At oral argument, the Commission reaffirmed its ruling (R. 3499), and the position statements were received without objection. (R. 3501, 3550, 3567, 3571)

the specific adjustments themselves.¹²

In its position statements, USWC made three basic points: (1) the Stipulation clearly and explicitly contemplated normalization adjustments of the financial results provided in the last six months of the year; (2) the adjustments proposed by USWC are appropriate normalization adjustments under general public utility law and are consistent with past decisions of the Utah Commission; and (3) the failure to make the adjustments would violate the Commission's goal of developing a test year that is representative of future operations. (R. 8322-27, 8346-49)

¹²While USWC is not asking the Supreme Court to decide whether the adjustments should be approved, it may be helpful to briefly describe the proposed adjustments. The adjustments proposed by USWC fell into three categories:

1. 1989 Tax True Up. During 1989, USWC made an accrual of its estimate of federal and state income taxes that would need to be paid in 1990 upon completion of the 1989 tax returns. When the returns were completed in September 1990, it became clear that USWC had over-accrued for 1989. The amount of the over-accrual was reversed in November 1990, thus causing the taxes for the 1990 test period to be understated. To correct this problem, USWC proposed to remove (i.e. normalize) this entry from the test period since it related to a prior period. (R. 8331-32, 8351-57)
2. Prior Period Tax Adjustments. This category consists of six separate tax items. All but one of them are accounting entries that are unrelated to the 1990 test year. One of them was an expense which terminated in 1990 and would not be in effect in 1991 or years thereafter. (R. 8328-29, 8357-61)
3. Prior Period Depreciation. This adjustment related to 1990 depreciation entries that related to prior periods. (R. 8334-35, 8361-65)

The adjustments totalled \$5.916 million. (R. 8379) The Division opposed the 1989 tax true-up adjustment, supported all but one of the prior period tax adjustments, and agreed with portions of the prior period depreciation. The net amount of total adjustments supported by the Division was \$2.197 million. The Committee opposed all adjustments. (Id.)

The Division agreed with USWC that the Stipulation contemplates normalization adjustments to the financial results in the last six months of the year, although the Division did not agree that all the adjustments proposed by USWC should be accepted by the Commission. The Division viewed the language in the Stipulation contemplating normalization adjustments as being an integral part of the Stipulation, which should be given effect by the Commission.¹³ On the other hand, without even addressing the normalization language in the Stipulation, the Committee asserted that no adjustments to actual test year data were allowed by the Stipulation. (R. 6041-58)

In its Order, the Commission refused to even consider the adjustments and the detailed evidence on record, finding that "the new adjustments proposed by the Company are not permitted by the terms of the Stipulation and are therefore rejected." (R. 5392) In its Order on Review, the Commission reiterated the same conclusion. (R. 5697-98)

B. Modernization Issues. Contingent upon approval of an incentive regulation plan acceptable to it, USWC proposed to make the following network modernization upgrades over a 54-month period:

¹³ In its second position statement, the Division stated:

USWC in its filing has outlined its view of normalization and annualization adjustments. They have stated that they believe the Stipulation provides that the six months of data presented to the Commission at the time of the Stipulation should be updated and annualized and normalized as were the first six months data. The DPU has no disagreements with this concept and so stated in its original filing. (R. 7184) (emphasis added).

- Central Office Upgrades. Upgrade the 41 remaining electromechanical central offices (together with associated network upgrades) at a cost of \$36 million.
- Digital Backbone Facilities. Place fiber optic and digital microwave facilities from Nephi to St. George at a cost of \$23 million.
- Distance Learning Facilities. Place the necessary facilities to build a network that could support distance learning and other services to colleges and universities in Utah at a total cost of \$32.4 million. (R. 7784-86, 7828, 7924, 7926-27)

The Division and Committee took positions similar to each other regarding these three aspects of the plan. Both took the position that the central office upgrades should be ordered by the Commission, irrespective of whether USWC agreed to an incentive regulation plan. (R. 6107-12, 6778, 6944-50) However, neither proposed that USWC be ordered to place the digital backbone or distance learning facilities. In fact, both parties opposed ordering the fiber backbone and distance learning facilities as part of an incentive regulation plan. (R. 6551, 6657, 6957-60)

In its order, the Commission found that "service to certain customer areas is not adequate by present day standards," (R. 5459-60) and ordered USWC to implement all three aspects of the modernization proposal, irrespective of whether USWC accepted the incentive regulation plan proposed by the Commission. (R. 5461-62)

1. **Evidence in the record supporting a finding that electromechanical central offices provide inadequate service.** The vast majority of the evidence on modernization issues presented at the hearing related to the central office

upgrades. As will be discussed below, USWC challenges the Commission's finding of inadequate service, particularly with regard to the central office upgrade issue, on the ground that the finding is not based on substantial evidence in the record. USWC is cognizant that, in challenging the Commission's inadequacy finding on substantial evidence grounds, it has a duty to "marshall all of the evidence supporting the findings and show that despite the supporting facts, and in light of the conflicting or contradictory evidence, the findings are not supported by substantial evidence." Grace Drilling Co. v. Board of Review, 776 P.2d 63, 68 (Utah App. 1989); First Nat'l Bank v. County Board of Equalization, 799 P.2d 1163, 1165 (Utah 1990). Therefore, in order to meet its duty under the marshalling rule, USWC shall hereafter attempt to set forth the evidence in the record that supports a finding of inadequacy of service.¹⁴

In the hearings, a considerable amount of testimony and other evidence was presented relating to whether USWC should be required to upgrade the electromechanical central offices with the newer digital electronic technology. The evidence in support of the claim that the existing technology is inadequate related exclusively to the service benefits that would result from new central offices.

There are two kinds of electromechanical offices: (1) step-by-step (commonly referred to as "SXS") and (2) cross-bar (commonly referred to as "X-

¹⁴As discussed in Sections II.A, II.B, and II.C, *infra*, USWC contends that the lack of adequate findings makes it essentially impossible for USWC to marshal the evidence.

Bar"). (R. 6939) Electromechanical central offices were developed in the 1940s and 1950s. They rely on the movement of electromechanical switches in the central office in order to direct a call from one caller to another. Beginning in the late 1960s and early 1970s, telephone companies, including USWC, began installing computer based analog electronic central offices. Id. Since the early 1980s, the state-of-the-art technology for central office switching has been digital electronic central offices. Id., (R. 8109) All witnesses agreed that the newer state-of-the-art central offices allow more accurate processing of dialed digits, faster touch-tone signal handling, faster call completion, clearer telephone conversations, and improved data transmission accuracy. (R. 6117, 6511-12, 6940, 6942-43, 7786, 8129) Mr. Fuller, the Division's witness, identified several services that are unavailable in electromechanical offices that are available in the newer technologies, such as custom calling features (call waiting, call forwarding, three-way calling and speed dialing). (R. 6943, 7796)¹⁵ USWC's witnesses readily acknowledged that all services available from electronic offices are not available from electromechanical offices. (R. 7796, 8128) On the other hand, the evidence was undisputed that electromechanical central offices provide the basic telephone services: basic

¹⁵ Mr. Fuller stated:

Customers served by SXS offices do not have the options for having basic or enhanced custom calling features and services, lower priced local exchange message rated services, remote call forwarding, custom intercept services, call restriction or blocking for 976 or 900 numbers, CENTRON services, Direct-Inward Dialing, all 800 subscription services, SDN, ISDN and other services readily available to over 90 percent of the other USWC customers. (R. 6943)

exchange service, extended area service,¹⁶ in-state long distance, and access to interstate long distance carriers.¹⁷

There was general agreement that electronic central offices are more trouble free than the electromechanical central offices; thus, customer trouble reports are less frequent in an electronic central offices than in electromechanical offices. (R. 6942-43, 8128)

Thus, the evidence supports the conclusion that there are general service benefits to customers from electronic central offices in terms of faster dialing and clearer transmission quality, that there are additional services available to customers from them, and that they are more trouble free.

2. Evidence relating to the economics of the central office upgrades. An issue related to whether the central office upgrades are economical surfaced during the hearings and became the subject of considerable testimony. USWC

¹⁶ Extended Area Service (EAS) allows calling between different central offices without an additional charge per call. For example, a Bountiful customer can make a call to a Salt Lake City customer without a long distance charge. Instead, as a part of the basic monthly charges, the customer pays a flat charge that covers calling within his or her EAS area.

¹⁷ Mr. Dunkel, the Committee's witness, agreed that both electromechanical and electronic central office provide basic dial tone, touch-tone service (the ability to use the faster dialing associated with a touch-tone keypad as opposed to the old dial-tilt phones), extended area service, and access to toll carriers. He also agreed that, while an electromechanical office has difficulty handling high speed data transmission, lower speed computer transmissions are feasible from an electromechanical office. (R. 2211-13, 2230)

took the position that the upgrade of all offices would be uneconomical.¹⁸ The Committee concluded they were economical. (R. 6234-35, 6511, 6555-57) The Division agreed with USWC that they were uneconomical,¹⁹ but nevertheless urged the Commission to order the upgrades. The Commission, while ordering the upgrades, concluded that the evidence was inconclusive and found that it was unable to "conclude that the proposed central office upgrade is uneconomical." (R. 5457)

Because of the legal implications of the Commission's refusal to consider USWC's evidence on the economics of the upgrades,²⁰ it is important to understand the facts relating to this issue. USWC presented extensive testimony describing its methodology for determining when it makes economic sense to replace existing facilities with newer technology. (R. 8113-18, 8166-69) Under this

¹⁸Selander Surrebuttal Testimony, at 13-19 and exhibits 7SR.1 to 7SR.7. This testimony and exhibits are attached hereto as Addendum D. Due to an apparent oversight, Mr. Selander's surrebuttal testimony was not included in the record on appeal. Counsel for the Commission, Division, and Committee orally agreed that it could be attached as an Addendum to this Brief.

¹⁹In its brief to the Commission, the Division acknowledged that upgrading the offices would not be economic:

The economic studies presented show that it is not economic from the Company standpoint to convert these offices. That is no surprise. As more and more offices are converted, what will be left will be those that have the worst economics.

(R. 5216, footnote 23) On cross-examination, Mr. Fuller reached the same conclusion. (R. 2528-29)

²⁰ See Section II.D, infra.

process, the Company compares the present method of operation ("PMO") to other alternatives. Id. These kinds of analyses are done most commonly when the Company is faced with the absolute need to make a decision. For example, if the copper lines linking two central offices are nearing an exhaustion point, the Company will analyze whether it should reinforce those lines with additional cable or supplement or replace it with fiber optics or microwave. When a central office is nearing its exhaustion point, the Company will analyze whether to add onto it with the same kind of technology (i.e., add additional electromechanical equipment) or completely replace it with newer technology. The kinds of events that trigger the need to analyze alternatives are commonly called "hard triggers." (R. 8114) The testimony of USWC witnesses was that, while some of the 41 central offices would encounter hard triggers in the next few years that would dictate replacement, for most of them no hard trigger was anticipated in the foreseeable future. (R. 7794, 8169-71) However, as part of an acceptable incentive regulation plan, USWC was willing to commit to their replacement in advance of hard triggers that would dictate replacement on economic grounds. (R. 8171) Because of USWC's willingness to do the upgrades as part of an acceptable incentive plan, USWC performed no specific economic study of the 41 offices before proposing the plan. (R. 7022-23)

Messrs. Fuller and Dunkel, the witnesses for the Division and Committee, outlined specific cost savings or other economic benefits that would come from replacement of the central offices, such as lower maintenance expense, less

power consumption, the elimination of the need for digital analog conversion equipment, easier and less expensive testing procedures and less of a need to dispatch personnel for trouble detection. (R. 6549-50, 6940-43) Both witnesses also testified that there were greater revenue opportunities from the newer central offices. (R. 6550, 6949-50) Mr. Fuller, however, did not claim that the existence of these factors made the central office upgrades an economic decision. He acknowledged that, in determining whether an upgrade was an economic decision, all factors should be brought together to make an overall determination (R. 2541-42) and that USWC's study methodologies bring these factors together. (R. 2542) Mr. Dunkel acknowledged that the overall economic decision must be based on a consideration of all factors, including new revenues, maintenance savings, cost of replacement, and other relevant factors (R. 2208), and noted that the piece of equipment that costs the least overall is the one that is most efficient. (R. 2209) Mr. Selander testified that many factors must be weighed together to determine the most economic alternative. (R. 8116)

Through discovery, the Committee sought information from USWC relating to the overall economics of the central office upgrades. (R. 7022-28) Although no specific economic study of the 41 central offices had been done (R. 7025), in an effort to be responsive, USWC provided information from 1988 based on a generalized study of a much larger list of central offices. *Id.* Based on that information it appeared that the replacement of some of the offices would be economical, some would clearly be uneconomical, and on the whole, it appeared

that the entire package was "marginally economical, but suboptimal."²¹ (R. 6208) Mr. Dunkel made the claim in his rebuttal testimony that the overall central office upgrade plan was an economic decision. (R. 6511, 6555-57) In response to those assertions, and because no specific study of the 41 offices had been done, USWC performed a specific economic study of the 41 central offices to determine if the central office upgrade project was economical. (R. 7028-29, Selander Surrebuttal at 12-13, Addendum D) The results of that study were presented in the surrebuttal testimony of USWC witness Selander. The conclusion of the specific study was that the central office upgrades as a whole would be uneconomic. (Selander Surrebuttal at 12 and Exhibits 7SR.1 to 7SR.7, Addendum D)

3. Commission findings regarding central office upgrades. In its order, the Commission made only two factual findings specific to the central office upgrade issue. The first finding states:

The Commission finds that the central office upgrades will provide more accurate processing of dialed digits, faster touch-tone services, faster call completion, clearer conversations and more accurate data transmissions. The Commission further finds that the modernization plan will enable USWC to provide newer services that are not currently available in Utah.

²¹ Mr. Williams explained the meaning of these terms in the following manner:

If a "package" is economical overall, but the economies of most of the components of the package lie at or very near the 'break-even' point, the proposal is marginally economical. . . . Such a package would also be clearly "suboptimal", because a much more economical package could be constructed by including only those components that are clearly economical. Components that are "clearly economical" would be those that are far enough from the break-even point to remain economical even if revenues and expenses vary by twenty to thirty percent from the projections. (R. 7030)

(R. 5452)

The other finding specific to the central office issue relates to the economic studies discussed by Committee Witness Dunkel and USWC witnesses Selander and Williams:

The Commission finds that the Company's studies are not conclusive and may not include all of the benefits identified on the record, and therefore the Commission cannot conclude that the proposed central office modernization is uneconomical. (R. 5457)

The other finding relevant to the central office upgrade issue is the more general inadequacy finding:

The Commission finds that service to certain customer areas is not adequate by present day standards and that the modernization program is necessary at this time to provide all customers in this state with adequate and convenient service. (R. 5459-60)

On the basis of these findings, the Commission ordered USWC to upgrade the 41 central offices within 54 months of the date of the Commission's order.²²

4. **Evidence relating to the digital backbone and distance learning facilities.** As part of its proposed incentive regulation plan (and contingent upon the adoption of a plan acceptable to USWC), USWC proposed to place a fiber optic and digital microwave link between Nephi and St. George and to place the necessary facilities to support distance learning services. (R. 7784-86, 7828, 7924, 7926-27) In their testimony, USWC witnesses testified that these network enhancements would be generally beneficial.

²²Commission's Order dated June 19, 1991. Therefore, the 54-month period will end on December 19, 1995.

Unlike the positions they took regarding central office upgrades, the response of the Division and Committee to these proposals was decidedly cold. The Division took the position that the fiber optic facilities should only be upgraded "provided there are foreseeable demands for customer service or network survivability requirements to justify the investments." (R. 6957) As to the distance learning facilities, the Division stated that approval of them "as part of an incentive . . . plan, is not appropriate." (R. 6958) Thus, the Division concluded that any evaluation or approval of distance learning investments should take place "separate from the incentive plan." (R. 6960) Dr. Compton, another Division witness, testified that, "as regards the fiber/educational network the investment should not be made until a business prudence standard is met. That means the investment should not be made until it indeed would be compensatory." (R. 6657) The Committee's witness quoted Dr. Compton's statement in his testimony, indicating that "[t]he Division position is similar to our position." (R. 6551) Neither the Division nor Committee made any claim of inadequacy of service.

Several public witnesses presented testimony touting the general benefits of placing these facilities. (R. 2594-2600, 2612-16, 2625-53, 2660-65, 2679-83) None of them, however, argued that the Commission should order the upgrades in the absence of an incentive regulation plan.

The Commission found that "existing services are no longer adequate" and that "it is appropriate to order the Company to provide . . . fiber optic extensions." (R. 5461) The Commission also ordered USWC to "work with the Division and

various interested educational interests in the state to devise a program entailing the investment for extending fiber to these institutions as part of the total modernization plan," although the Commission also stated that "before construction is authorized," the educational "[i]nstitutions should be required to sign contracts, or otherwise demonstrate that they will utilize the fiber optic service and pay the rates determined." (R. 5462)

SUMMARY OF THE ARGUMENT

A. Stipulation Issues.

1. The revenue Stipulation entered by the parties and approved by the Commission explicitly provided that USWC's financial results for the last six months of the 1990 test period would be subject to "normalization" adjustments before the final revenue requirement was set.

2. The term "normalization" has a clear and explicit meaning in the context of utility regulation. It refers to the elimination of abnormal or non-recurring financial accounting events from a test year so that it serves as a reasonable proxy for the financial condition of the utility for the time that rates will be in effect. Normalization adjustments have routinely been approved by the Utah Public Service Commission in past orders.

3. Stipulations are interpreted under the law of contracts. In concluding that the Stipulation precluded the Commission from even considering USWC's proposed adjustments, the Commission violated USWC's rights under the Stipulation by failing to give meaning to the clear and explicit language of the

Stipulation. In so doing, the Commission violated the basic principle of contract construction that effect should be given to the entire agreement, without ignoring any part. Furthermore, the Commission's refusal to consider the adjustments ignored the clear intent of the Stipulation and failed to take into account the nature and purpose of the Stipulation, which was to create a representative test period for rate-setting purposes.

B. Modernization Issues.

1. Orders of administrative agencies must contain adequate findings of fact. Reliance solely on "ultimate" findings without subordinate findings sufficient to demonstrate that there is a logical and legal basis for the ultimate conclusion renders an order inadequate and incapable of meaningful review. Furthermore, the absence of sufficiently detailed subordinate findings makes it impossible for a petitioner to marshal the evidence and forecloses a petitioner from challenging an agency's undisclosed logic or undeclared interpretation of the law.

2. In this case, the Commission made the ultimate finding that "service to certain customer areas is not adequate under present day standards." With regard to all modernization issues (central office upgrades, fiber optic backbone, and distance learning facilities), the Commission failed to provide sufficient subsidiary findings to support its ultimate conclusion that service is inadequate. Furthermore, in failing to define "present day standards" or to specifically delineate the "customer areas," the Commission's findings neither disclose the

logical process used by the Commission in reaching its decision nor does it allow USWC to challenge effectively the undefined standards adopted by the Commission.

3. The failure of the Commission to provide sufficient subsidiary findings makes it impossible to USWC to marshal the evidence. Nevertheless, USWC has made an effort to do so. USWC's analysis of the facts that could conceivably support a finding that electromechanical central offices are inadequate demonstrate that, while there are differences between the level of service provided by electromechanical and electronic offices, there is a dearth of substantial evidence in the record to support the conclusion that service from electromechanical offices is legally inadequate. Thus, the Commission's inadequacy finding is not supported by substantial evidence.

4. A Utah case and prior Commission action demonstrate that a necessary issue to be considered in determining adequacy of service relates to the economic viability of upgrading service. In the case below, USWC presented the only specific economic study of the 41 central offices. That study demonstrated that the upgrade of the 41 central offices is not economic. The study was filed in full conformity with the schedule in the case and was received into evidence. Yet, in its order, the Commission concluded that the study was not timely filed and that the other parties had no opportunity to adequately review it. On that basis, the Commission refused to rely on it to make a finding regarding the economics of the upgrade. The Commission's conclusion that the study was not timely filed

and that the parties could not adequately assess it are demonstrably incorrect. Thus, in refusing to consider the uncontradicted economic study, the Commission acted arbitrarily and capriciously.

5. With regard to the fiber backbone and distance learning facilities, no party requested that USWC be ordered to deploy them in the absence of an acceptable incentive regulation plan. Indeed, no party presented any evidence in support of ordering the deployment. Both the Division and Committee argued that such investments should not be ordered in this case. Nevertheless, the Commission ordered USWC to make these investments, even in the absence of an incentive regulation plan. In so doing, the Commission violated USWC's due process rights by granting relief that was neither raised nor tried in the hearing below.

ARGUMENT

I. THE COMMISSION'S REFUSAL TO CONSIDER USWC'S PROPOSED NORMALIZATION ADJUSTMENTS TO THE TEST YEAR FINANCIAL RESULTS WAS CLEAR ERROR.

In the Stipulation, the parties agreed that the original JE-1 attached to the Stipulation had been calculated "using six months actual results which have been annualized and normalized . . ." (R. 4571, emphasis added) In paragraph 6 of the Stipulation, the parties agreed that in the upcoming December hearings²³ the

²³At the time the Stipulation was entered all revenue requirement issues were scheduled to be heard in December 1990. Those hearings were later continued until March 1991.

parties would update with “nine months actual results on an annualized and normalized basis consistent with the annualization and normalization of six months actual data in JE-1. (R. 4573, emphasis added) It is beyond dispute that the language of the Stipulation contemplated that the actual financial results for the last six months of 1990 would be “normalized.” Thus, the question that must first be addressed is to determine what “normalization” means in the context of the Stipulation.

A. The term “normalization” has a clear and explicit meaning that the Commission has utterly ignored. Furthermore, the Commission has routinely made normalization adjustments in past USWC rate cases.

Despite the facts that the Stipulation clearly calls for the “normalization” of the actual financial results for the last six months of 1990 and that both the Division and USWC reached the conclusion that USWC could propose the adjustments under the terms of that language, the Commission failed in its order to even address the meaning of “normalization”. Instead, the Commission focused on other issues²⁴ and ignored the plain language of the Stipulation.

Utah follows the well accepted rule of construction that “[w]hen terms used in a contract appear to have a specialized meaning, they must be understood in accordance with the particular connotation they may have acquired in such transactions.” Holland v. Brown, 394 P.2d 77, 78-79 (Utah 1964). The meaning of the term “normalization” in the context of utility ratemaking must, therefore, be addressed. Normalization is a regulatory accounting concept. The essence of the

²⁴ These issues are addressed in Section I.B., infra.

concept is that the actual reported financial information of a utility must often be adjusted in order to create a representative test year for ratemaking purposes. In other words, the test year must be adjusted to remove items that appear on the financial books in the test year, but which should not be considered for prospective ratemaking purposes. Thus, under the normalization concept, items that are booked in a test year but which relate to a prior period are removed. Similarly, items that occur during the test year, but which will not continue beyond the test year (and which therefore will not be effect during the period of time that rates are to be in effect), also should be removed. Hahne and Aliff, the leading authorities on public utility accounting in this country, define normalization adjustments this way:

Normalization adjustments are usually made to revenues or to expenses to compensate for unusual levels of operations as recorded during the period. The events that lead to normalizing adjustments are often extraordinary and non-recurring.

R.L. Hahne and G.E. Aliff, Accounting for Public Utilities, § 7.05 at 7-8 (1989).

One of the clearest statements of the underlying concept of normalization is set forth in Washington Utilities and Trans. Comm'n v. Pacific Power & Light Co., 7 P.U.R. 4th 470 (Wash. P.S.C. 1974):

First, the test-year selected reflects an actual year's experience by a company. The revenues received from customers are the revenues actually earned by the company. The operating expenses, depreciation, taxes, as well as federal income taxes, are the result of generating these actual revenues; the net operating income is the resultant actual experience. Likewise the company requires some actual amount of average net investment in utility plant in service plus working capital in order to generate these actual revenues.

Secondly, as rates are set for the near term future, and as infirmities may exist in actual record keeping, an immediate past actual year usually requires correction and reshaping before it is useful for rate-making purposes. Both company and staff by this process seek to arrive at a measurement of earnings expressed as a rate of return on investment before application of proposed rates.

The selection of a recently past actual year as a test year and the making of restating, normalizing, and pro forma adjustments to such a test year is an approach that this commission has adopted in innumerable cases involving public utility as well as transportation industries. Although various specific adjustments proposed to the test year by the parties usually are treated on individual merit in specific cases, the commission recognizes certain fundamental concepts in this pro forma test-year approach.

A most fundamental concept is that revenues, expenses, net operating income, and investment have an interrelationship and that this interrelationship is depicted by the actual year selected for test-year purposes.

Id. at 476 (emphasis added).

State v. North Carolina ex. rel. Utilities Comm'n. v. Carolina Power & Light Co., 358 S.E. 2d 35 (N.C. 1987), was a case in which “[a] major area of dispute during the hearings . . . involved the concept of normalizing the nuclear capacity factor component of CP&L’s test period generation mix.” Id. at 39. In addressing the dispute, the Court stated it previously had “given its specific approval to the process of normalizing” such disputed data. The Court then stated that the practice of “normalizing” complied with the North Carolina statutory requirement that the Utility Commission “adjust test period data to reflect abnormalities which had a probable impact on the utility’s revenues and expenses during the test period.” Id.

The normalization concept, whether specifically referred to as

“normalization” or not, is inherent in virtually all utility decisions involving the construction of a test year. Mountain States Telephone and Telegraph Co. v. Public Utilities Comm’n, 513 P.2d 721, 724 (Colo. 1973); Central Louisiana Electric Co. v. Louisiana Public Serv. Comm’n, 508 S.E. 2d 1361, 1369 (La. 1987); State of North Carolina ex rel. Utilities Comm’n v. Thornburg, 342 S.E. 2d 28, 37-38 (N.C. 1986); South Carolina Pub. Serv. Authority v. the Citizens and Southern Nat’l Bank, 386 S.E. 2d 775, 781 (S.C. 1989). While not using the term “normalization,” the Louisiana Supreme Court recently described the concept of adjusting actual financial results in order to create an appropriate test year:

There are two types of adjustments that are made to test year data: in-period adjustments and out-of-period adjustments. In-period adjustments are those necessitated by abnormal operating conditions in the test year which cause revenues and expenses or both not to reflect faithfully normal conditions. . . . Conversely, out-of-period adjustments are necessitated by changed operating conditions which are not reflected in the test year data.

Central Louisiana Elec., 508 S.E.2d at 1369 (emphasis added). The Colorado Supreme Court also has described the normalization process:

The relationship between costs, investment, and revenue in the historic test year is generally a constant and reliable factor upon which a regulatory agency can make calculations which formulate the basis for fair and reasonable rates to be charged. These calculations obviously must take into consideration in-period adjustments which involve known changes occurring during the test period which affect the relationship factor. Out-of-period adjustments must be also utilized for the same purpose.

Mountain States, 513 P.2d at 724 (emphasis added). These cases are among an overwhelming number that stand for the proposition that adjustments to test period data must be made in order to develop a representative test period for ratemaking purposes. E.g., Gulf Power v. Bevis, 289 So. 2d 401 (Fla. 1974);

Southern New England Telephone Co. v. Public Utilities Comm'n, 282 A.2d 915, 918-19 (Conn. Super. Ct. 1970); Mountain States Telephone and Telegraph Co. v. New Mexico Corp. Comm'n, 563 P.2d 588, 603 (N.M. 1983).

The record also demonstrated that these kinds of adjustments have been made and routinely approved by the Commission in past USWC rate cases. USWC noted in one of its position statements that in the prior USWC rate case seven normalization adjustments were made by agreement of all parties. Of the seven adjustments, five increased and two decreased the revenue requirement. Given the larger size of the two adjustments that decreased the revenue requirement, the net impact of all seven was a reduction to USWC's revenue requirement. (R. 8326-28) The Committee and Division agreed to each of these adjustments without objection.

The term "normalization" has a clear and a specific meaning in the context of the Stipulation. Consistent with that clear meaning, any party had a right under the Stipulation to propose adjustments to remove items inappropriately included in a test period. In full compliance with the Stipulation, USWC identified, explained and quantified several normalization adjustments to the financial results in the last six months of 1990, all of which was received as evidence by the Commission.

B. The Commission's conclusion that the Stipulation cannot allow the adjustments proposed by USWC violates several rules of construction applied by this Court.

Under Utah law, stipulations are to be interpreted based upon the

principles of contract law. Kinsman v. Kinsman, 748 P.2d 210, 212 (Utah App. 1988); Brown v. Brown, 744 P.2d 333, 334-35 (Utah App. 1987); Klein v. Klein, 544 P.2d 472, 476 (Utah 1975), United Factors v. T.C. Associates, Inc., 446 P.2d 766 (Utah 1968).

Several rules of contract construction are relevant in this case:

1. All parts of a contract should be given meaning and no portion should be ignored. Minshew v. Chevron Oil Co., 575 P.2d 192 (Utah 1978).²⁵
2. Contracts should be construed in accordance with their nature and purpose. Utah Medical Ass'n v. Utah State Employee's Credit Union, 655 P.2d 643, 646 (Utah 1982).²⁶
3. The purpose of contract construction "is to give effect to the intentions of the parties," which, to the extent possible, "must be determined from an

²⁵ The established rules of contract interpretation require consideration of each of its provisions in conjunction with the others and, if possible, to give effect to all. Effect is to be given the entire agreement without ignoring any part thereof.

Minshew, 575 P.2d at 194.

²⁶ In interpreting the terms of a contract, the Court must look to the agreement as a whole, to the circumstances, nature and purpose of the contract.

Utah Medical Ass'n, 655 P.2d at 646 (emphasis added). See also Big Cottonwood Tanner Ditch Co. v. Salt Lake City, 740 P.2d 1357, 1359 (Utah App. 1987) (A contract "should be looked at in its entirety and in accordance with its purpose").

examination of the text of the agreements.” Atlas Corp. v. Clovis Nat. Bank, 737 P.2d 225, 229 (Utah 1987).

The application of these principles to the issues in this case demonstrate that the Commission erred.

1. **The Commission failed to give meaning to the language of the Stipulation.**

It is beyond dispute that the Stipulation contemplates the “normalization” of the last six months data in 1990. As demonstrated above, that language has a clear and specific meaning in utility ratemaking. Instead of examining the meaning of that term, the Commission reached the startling and unsupported conclusion that “[t]he intent of the signatory parties to rely on the Stipulation as crafted and to exclude consideration of further adjustments is made clear in paragraphs six and seven of the Stipulation.” (R. 5389)

The irony of the Commission’s reference to paragraph 6 is that it is in that paragraph where the parties agreed that the additional financial results would be updated and normalized.

The Commission also stated that the parties intended to resolve all revenue requirement issues except depreciation and cost of capital. (R. 5388) While it is true that those two issues were reserved, it is clear error to conclude that every other conceivable issue was resolved. The Stipulation called for certain items to be updated and it specifically contained the agreement that the last six month’s financial results would be annualized and normalized. In so stating, the Stipulation obviously left the door open to specific proposals of the parties as to how

that data should be normalized. The right to propose normalization adjustments was not a one-way street – all parties had the right to propose normalization adjustments to the last six month's financial results.²⁷ The Commission's interpretation of the Stipulation is irreconcilably inconsistent with the unambiguous "normalization" language in the Stipulation and fails to give effect to a material provision of the Stipulation. Normalization has a specific and identifiable meaning. The Commission's interpretation of the Stipulation utterly negates the term in the Stipulation and renders it meaningless. By ignoring the normalization language, the Commission failed to meet the requirement of Minsheu that "[e]ffect is to be given the entire agreement without ignoring any part thereof." 575 P.2d at 194.

Another reason given by the Commission was that "USWC proposed four new adjustments to test year data, on issues the other signatory parties had not seen at the time the Stipulation was signed and which had the effect of increasing revenue requirement." (R. 5390) The Commission is correct that none of the parties were aware of the adjustments when the Stipulation was signed, but the statement misses the point. The uncertainty at the time the Stipulation was entered is precisely why the "normalization" provision was included in the Stipulation – the parties did not have the last six months data and it was not known whether it would need to be adjusted to create a representative test period

²⁷ Normalization adjustments can obviously go both ways. In fact, the net effect of normalization adjustments in USWC's last rate case was a reduction of USWC's revenue requirement, thus benefitting ratepayers. (R. 8326-28)

for ratemaking purposes. The evidence presented by USWC was that the vast majority of the adjustments related to bookings in the last six months of the year, so that they were not in the results upon which the original JE-1 was based. (R. 8337, 8348) As with the Commission's other reasons for refusing to consider the adjustments, this one is also inconsistent with the legal requirement to give meaning to the terms of the agreement.²⁸

2. The Commission's interpretation of the Stipulation is inconsistent with its nature and purpose.

The purpose of the Stipulation was to develop a mechanism by which the revenue requirement of USWC could be established so that rates could be set on a prospective basis. One specific purpose was to assure that the test year data was appropriately normalized. That purpose, of course, is crucial in the ratemaking process to assure that, as articulated by the Commission, the purpose of test year construction is achieved:

The purpose of a test year, or test period, is to provide revenue, expense and investment information that reasonably approximates circumstances expected during the period rates will be in effect.

In re Mountain Fuel Supply Co., Docket No. 89-057-15, at 6 (Utah P.S.C., November 21, 1990). The purpose of the normalization language of the Stipulation was to achieve that purpose. By refusing to consider the normalization

²⁸The Commission also reasoned that USWC's proposed adjustments were inappropriate because, by their very nature, stipulations involve negotiation, give and take, and the concession of certain issues. (R. 5391) That is true but inapplicable to the normalization adjustments. USWC certainly gave up issues that were not subject to later dispute – USWC agreed to several adjustments that it would otherwise have litigated. However, neither USWC nor any other party gave up the right to propose normalization adjustments.

adjustment, the Commission failed to interpret the Stipulation in accordance with its nature and purpose as required by the holdings in Utah Medical Ass'n, 655 P.2d at 646, and Big Cottonwood, 740 P.2d at 1359.

3. **The Commission's interpretation of the Stipulation inappropriately ignores the clear intent of the parties.**

In reaching its conclusion, the Commission stated:

There has also been some discussion about what the parties could, did, or should have understood was contemplated by the Stipulation. At this point in time, all that is important is what the Commission understood to be stipulated to by the parties at the time it accepted its Stipulation. None of the adjustments now argued for by USWC or the Division were considered open issues by the Commission. (R. 5391, emphasis added)

The Commission thus presents a novel theory of contractual interpretation: regardless of the literal language of the Stipulation, the determinant of its meaning is what the Commission subjectively understood. Needless to say, such a theory is not supported by the law. Utah, like virtually every other state, follows the standard that, in construing a contract, a court "is to give effect to the intentions of the parties," which "if possible . . . must be determined from an examination of the text of the agreements." Atlas Corp., 737 P.2d at 229. The subjective intent of the parties, not to mention the subjective intent of the court (or in this case, the Commission), is utterly irrelevant if it conflicts with the objective meaning of the contract.

C. Summary.

In refusing to consider the normalization adjustments, the Commission has substantially prejudiced the rights of USWC granted by the Stipulation. The

Commission's interpretation of the Stipulation constitutes an erroneous interpretation and application of the law. Utah Code Ann. § 63-46b-16(4)(d). Furthermore, the Commission has acted contrary to its prior practices with no demonstration of a fair and rational basis for the inconsistency. Utah Code Ann. § 63-46b-16(4)(h)(ii).

USWC therefore requests that this Court reverse the Commission's refusal to consider the normalization adjustments proposed by USWC, remand the matter to the Commission with the direction to consider those adjustments, and to require that, to the extent the adjustments are accepted, USWC be allowed to recover from ratepayers the revenues it should have received had the Commission correctly interpreted and applied the Stipulation.

II. THE COMMISSION'S ORDER REQUIRING USWC TO UPGRADE 41 CENTRAL OFFICES IS IN ERROR FOR SEVERAL REASONS AND MUST BE REVERSED.

A. The Commission's finding that the service provided from the 41 electromechanical central offices is inadequate is not based on sufficient subsidiary findings.

In the Commission's order, the findings of fact and conclusions of law are the portions set forth in bold print.²⁹

The ultimate findings upon which the Commission premised its Order requiring the central office upgrades are the following:

²⁹ Because the order was not totally clear as to what constituted the findings of fact and conclusions of law, counsel for USWC sought clarification from the Commission at a hearing held on July 1, 1991. The Chairman of the Commission agreed that the findings and conclusions are the portions in bold print. Attached hereto as Addendum E is the portion of the transcript of July 1, 1991 addressing this issue.

The Commission finds that service to certain customer areas is not adequate by present day standards and that the modernization program is necessary at this time to provide all customers of this state with adequate and convenient service. It is, therefore, in the public interest. . . . (R. 5459-60, emphasis added)

The other ultimate finding with regard to central office upgrades is similar:

The Commission finds that existing services are no longer adequate and concludes that the modernization plan is justified in that it brings telecommunications in Utah in line with present day service expectations. Therefore, it is appropriate to order the Company to provide central office upgrades estimated at a cost of \$36.35 million (R. 5461, emphasis added)

While the Commission does not explicitly so state, it appears that these findings of "inadequacy" are premised on Utah Code Ann. § 54-4-7, which states in relevant part:

Whenever the Commission shall find, after hearing, that the rules, regulations, practices, equipment, appliances, facilities, or service of any public utility or the methods of manufacture, distribution, transmission, storage or supply employed by it, are unjust, unreasonable, unsafe, improper, inadequate, or insufficient, the Commission shall determine the just, reasonable, safe, proper, adequate, or sufficient rules, regulations, practices, equipment, appliances, facilities, service or methods to be observed, furnished, constructed, enforced or employed, and shall fix the same by its order, rule or regulation. (emphasis added)

The only other findings made by the Commission relating explicitly to the central offices are (1) the finding that the economic studies relating to the central office upgrades are inconclusive³⁰ and (2) the following finding relating to the benefits of upgrading the central office technology:

The Commission finds that the central office upgrades will provide more accurate processing of dialed digits, faster touchtone services, faster call completion, clearer conversations and more accurate data transmissions.

³⁰ This issue is discussed in Section II.D, infra.

The Commission further finds that the modernization plan will enable USWC to provide new services that are not currently available in Utah. In addition, the Commission finds that the proposed investments would be of benefit to and would meet a wide variety of residential, business, educational, governmental and research needs, and concludes that the Company's proposed modernization program is clearly in the public interest. (R. 5452)

This finding is the only one made by the Commission that even peripherally addresses the question of service adequacy from the electromechanical central offices. It merely repeats the consensus of all of the parties that there are general benefits that will inure to customers from the upgrade of central offices. Those facts, however, do not logically constitute a necessary threshold determination that electromechanical central offices are presently inadequate. It merely establishes that there are differences between the two types of central offices. Thus, the question is whether that finding constitutes a sufficient subsidiary finding to support the Commission's ultimate factual conclusion that the electromechanical central office facilities are inadequate.

Three Utah appellate decisions are directly relevant to the issue of the reviewability of decisions of administrative agencies that lack sufficient subsidiary findings.

The first case is Mountain States Legal Foundation v. Public Serv. Comm'n, 636 P.2d 1047 (Utah 1981). In Mountain States, this Court outlined several general principles relating to findings of fact. The first is the principle that "the Commission must make findings of fact which are sufficiently detailed to apprise the parties and the Court for the basis of the Commission's decision."

Id. at 1051. The Court also stated:

For this Court to sustain an order, the findings must be sufficiently detailed to demonstrate that the Commission has properly arrived at the ultimate factual findings and has properly applied the governing rules of law to those findings. Ultimate findings as to reasonableness and discrimination must be sustained if there are adequate subordinate findings to support them, and there is substantial evidence to support the findings. . . . It is not the prerogative of this Court to search the record to determine whether findings could have been made by the Commission to support its order, for to do so would be to usurp the function with which the Commission is charged.

Id. at 1052. Five years later, in Milne Truck Lines, Inc. v. Public Serv. Comm'n, 720 P.2d 1373, 1378 (Utah 1986), this Court re-emphasized the necessity of adequate subsidiary findings, concluding that the lack of them prevents the Court from performing its duty of reviewing an administrative agency's order:

The Commission cannot discharge its statutory responsibilities without making findings of fact on all necessary ultimate issues under the governing statutory standards. It is also essential that the Commission make subsidiary findings in sufficient detail that the critical subordinate factual issues are highlighted and resolved in such a fashion as to demonstrate that there is a logical and legal basis for the ultimate conclusions. The importance of complete, accurate, and consistent findings of fact is essential to a proper determination by an administrative agency. To that end, findings should be sufficiently detailed to disclose the steps by which the ultimate factual conclusions, or conclusions of mixed fact and law, are reached. . . . Without such findings, this Court cannot perform its duty of reviewing the Commission's order in accordance with established legal principles and of protecting the parties and the public from arbitrary and capricious administrative action.

Id. (citations omitted, emphasis added).

A decision of the Court of Appeals further developed these basic principles. In Adams v. Board of Review, 821 P.2d 1 (Utah App. 1991), the Court of Appeals reviewed an order of the Industrial Commission denying benefits. In its order,

the Commission had simply concluded that the claimant had “failed to prove causation,” without making any supporting factual findings. The Adams court engaged in a lengthy review of the legal authority cited above as well as other authorities. For example, the Adams court quoted Tolman v. Salt Lake County Attorney, 818 P.2d 23, 31 (Utah App. 1991), for the proposition that “[a]dministrative bodies may not rely upon findings that contain only ultimate conclusions.”³¹ The Adams court also noted that “a rehearsal of contradictory evidence does not constitute findings of fact,” and that “[w]hen multiple conflicting versions of the facts create a matrix of possible factual findings, we are unable on appeal to assume that any given finding was in fact made.” Adams, 818 P.2d at 6, 7. In concluding that the agency had failed to articulate adequate subsidiary findings, the Court articulately expressed the underlying reason why such findings must be made:

³¹ The Adams court also relied on Nyrehn v. Industrial Comm’n, 800 P.2d 330 (Utah App. 1990), cert. denied, 815 P.2d 241 (Utah 1991), where the Court of Appeals concluded that “material findings . . . may not be implied.” Id. at 335. The Nyrehn court went on to state:

In order for us to meaningfully review the findings of the Commission, the findings must be “sufficiently detailed and include enough subsidiary facts to disclose the steps by which the ultimate conclusion on each factual issue was reached.” Acton v. Deliran, 737 P.2d 996, 999 (Utah 1987) (quoting Rucker v. Dalton, 598 P.2d 1336 (Utah 1975)). The failure of a trial court to make adequate findings is reversible error. Id. Likewise, the failure of an agency to make adequate findings of fact on material issues renders its findings “arbitrary and capricious” unless the evidence is “clear, uncontroverted and capable of only one conclusion.” Id., quoting Kinkella v. Baugh, 660 P.2d 233, 236 (Utah 1983).

Id. at 335.

Once an administrative agency attempts to state its findings, identify the applicable law, and articulate its logic, it may discover that critical facts are not properly before it, that the law is other than anticipated, or that its initial logic is flawed. In such situations, a result contrary to the initial conclusions of the body may be dictated. The process of articulation clearly enhances agency self-discipline and protects against arbitrary and capricious decisions. Without the safeguard of adequate findings, there is no guaranty that the agency followed a logical process in reaching its decision. If on the other hand, the agency identifies the facts, law, and reasoning supporting its decision, it reveals its logical process and the parties can be assured that a logical process occurred, even if it is in some manner flawed.

If an agency's logical process is flawed, its shortcomings can be corrected on review, but only if the agency creates findings revealing the evidence upon which it relies, the law upon which it relies, and its interpretation of law. Absent adequate findings, a petitioner wishing to challenge an agency's factual findings will not be able to marshal the evidence in support of the findings. . . . Nor will a petitioner be able to challenge the agency's undeclared interpretation of the law or its undisclosed logic. . . .

If findings are inadequate, this Court will be unable to effectively and efficiently perform its duty of review. . . . It is axiomatic that the denial of Adams' claim without the possibility of meaningful review by this Court, as provided for by UAPA is clearly prejudicial.

Id. at 7-8 (emphasis added).

Under the principles enunciated in these cases, it is clear that the Commission's finding of inadequacy is flawed. The single subsidiary finding made by the Commission demonstrates merely that there are differences between the electromechanical and electronic switches and that the electronic switches provide certain positive benefits to customers. However, there is a complete dearth of findings to demonstrate that customers find these differences to be significant. While electronic central offices provide somewhat faster dialing and call completion, the Commission made no findings that the differences between

the offices are significant to customers or that the current level of service provided out of electromechanical offices is less than adequate.³² The mere identification of differences without any factual evidence demonstrating that the differences are important to customers renders such a finding meaningless. Further, while the evidence is undisputed that additional services may be provided from the electronic offices, other than noting that new additional services are available, the findings contained nothing to indicate that the additional services are being required or demanded in significant amounts by the customers served from those offices. There is certainly no finding that the additional services are essential to those customers.

The lack of subsidiary findings in support of the inadequacy finding makes the Commission's ultimate finding essentially unreviewable, thus constituting prejudicial harm to USWC.

B. The Commission's failure to define the standards by which it found that the electromechanical central offices are inadequate makes the finding so vague as to be unreviewable.

The Commission found that "service to certain customer areas is not adequate under present day standards" and that the "modernization plan is justified in that it brings telecommunications in Utah in line with present day service expectations." (R. 5459-60, 5461, emphasis added) Yet, nowhere in the order did the Commission make any effort to define either "present day standards" or "present day service expectations." The failure to provide a

³² For example, Mr. Fuller, the Division witness, acknowledged that slower dialling is "[n]ot really" significant to customers. (R. 2555)

definition of these standards makes it impossible to examine whether there is adequate evidence to support the finding of inadequacy.³³ Likewise, the Commission's failure to specifically delineate the "customer areas" suffers from the same deficiency.

Because of these shortcomings, it is impossible to determine whether "the agency followed a logical process in reaching its decisions." Adams, 821 P.2d at 8. It is also impossible to know what legal standard the Commission applied in determining its undisclosed adequacy standard. As the Adams court stated, where the findings are inadequate, the petitioner will not "be able to challenge the agency's undeclared interpretation of the law or its undisclosed logic." Id. Instead of clearly articulating a definition of "present day standards," the Commission found that "it is for this Commission to determine what is necessary and convenient in the way of utility services. . . ." (R. 5460) The problem, of course, is that without a definition of the standards that the Commission found USWC to have violated, the decision is unreviewable. The Commission's use of a subjective and unarticulated standard fails to allow USWC to challenge the Commission's "undeclared interpretation of the law or its undisclosed logic." Id.

³³ To the extent these "present day standards" are to be generally applicable in Utah, they would constitute rules under Utah law. Under the Administrative Rulemaking Act, rulemaking is required whenever the agency action "authorizes, requires, or prohibits an action" or "applies to a class of persons." Utah Code Ann. § 63-46a-3(2)(a) & (c). Certainly, these "present day standards" require action by USWC, as evidenced by the Commission's order requiring the deployment of the modernization investments. It would also appear that the standards would apply to all telephone utilities in the state. Because the Commission did not follow the procedures in the Rulemaking Act, the Commission's action is legally deficient.

Because these findings are unreviewable under the appropriate legal standards, the Commission has erroneously interpreted and applied the law, and its decision is arbitrary and capricious, all of which has substantially prejudiced USWC. Utah Code Ann. §§ 63-46b-16(4)(d) & (h)(iv).

C. **The Commission's failure to make sufficient subsidiary findings to support its inadequacy finding has made it impossible for USWC to marshal the evidence on this issue. Nevertheless, it is clear that the inadequacy finding is not based on substantial evidence.**

In the previous sections, USWC demonstrated that the Commission's inadequacy finding is not supported by sufficient subsidiary findings and is so vague as to be unreviewable. The Adams court made it clear that when an agency's findings are inadequate, "a petitioner wishing to challenge an agency's factual findings will not be able to marshal the evidence in support of the findings." 821 P.2d at 8. That is precisely the position in which USWC finds itself. There was a great deal of evidence presented on the issue of central office upgrades, most of which does not appear to be relevant to the adequacy of service issue. However, because of the obvious deficiencies in the Commission's findings, it is virtually impossible to marshal the evidence relied upon by the Commission.

Nevertheless, because USWC feels strongly that there is no substantial evidence in the record below to support a finding that service from the electromechanical central offices is inadequate, USWC (in sections B.1 and B.2 of its Statement of Facts) attempted to marshal the evidence that could conceivably support such a finding. A review of that evidence demonstrates that substantial evidence was lacking to support an inadequacy finding.

The evidence in the record that could conceivably support an inadequacy finding produces three basic factual propositions: (1) that service from electronic offices is better than from electromechanical offices, (2) that more services are available from electronic offices, and (3) that electronic offices are more trouble free. USWC does not dispute any of these propositions. However, the essential problem with the evidence is that, while it demonstrates differences between the technologies, it does not demonstrate that service from the electromechanical offices is inadequate. USWC's witnesses readily acknowledged the differences, but consistently stated that the levels of service in the electromechanical offices are more than adequate.³⁴ The mere demonstration of qualitative differences between two technologies does not necessarily compel the conclusion that the less advanced technology is inadequate. Reasonable people would acknowledge that a Mercedes will provide a smoother ride, greater performance, and more optional features than a Chevrolet, but those facts do not lead to the conclusion that a Chevrolet is inadequate as a means of transportation.

With one limited exception, there was no evidence from customers in any of the 41 central offices that service is inadequate.³⁵ The only testimony from the

³⁴ Mr. Selander, USWC's Director of Network Facilities Engineering, acknowledged the benefits of electronic switches but firmly stated that electromechanical switches are "still performing in Utah at acceptable performance levels." (R. 8128, see also 7795, 7883-84)

³⁵ Dale Porter, a non-party public witness, expressed some complaints on public witness day regarding the quality of service in Morgan, which is served by an electromechanical switch. (R. 2620-23) It would be totally inappropriate to condemn all 41 electromechanical central offices (or, for that matter, even the

parties came from Mr. Fuller, a Division staff member, and Mr. Dunkel, a resident of Illinois. Neither the Division nor Committee provided any testimony relating to service levels in any of the 41 central offices to support their claim of inadequacy. On the other hand, Mr. Selander presented un rebutted evidence that Public Service Commission complaints from customers in electromechanical offices in 1990 averaged 6.0 per 10,000 access lines while the rate from comparably sized electronic offices averaged 5.7 per 10,000 access lines. (R. 8217) He also testified that only nine of the complaints in 1990 related to the performance of the electromechanical offices. Those nine complaints came from customers in central offices serving over 66,000 access lines. (R. 8175) Mr. Selander also presented evidence relating to trouble reports from electromechanical offices. In August 1982, for all central offices (both electronic and electromechanical) there were 3.41 trouble reports per 100 lines on a monthly basis in Utah. In 1990, the trouble report rate for electromechanical offices alone had dropped to 2.86 per hundred per month. (Selander Surrebuttal at 8, Addendum D) Thus, while the trouble report rate in electromechanical offices is higher than in electronic offices, the un rebutted evidence showed that service in electromechanical offices has continued to improve and is lower than the trouble report rate in all central offices 1982. Service from electromechanical offices has continued to improve over time.

In USWC's previous rate case, Docket No. 88-049-07, the Division also

Morgan office) by extrapolating from the testimony of one witness.

proposed that the Commission order USWC to upgrade its electromechanical switches. The reasons cited by Mr. Fuller to support his position that service is inadequate in both Docket No. 88-049-07 and in the case below are virtually identical.³⁶ In Docket No. 88-049-07, the Commission concluded that "an aggressive replacement program at this time is not justified in the record in this docket."³⁷ Mr. Fuller acknowledged that the fundamental nature of digital and electromechanical switches did not change between his testimony the 1988 case and in the case below. (Tr. 2068)

While the Commission mentioned that more services are available from electronic switches (R. 5452), no party presented evidence that these services are

³⁶Compare Mr. Fuller's testimony in Docket No. 88-049-07 (R. 8316-19) to his testimony in this case. (R. 6940-44) Mr. Fuller acknowledged that he had merely replicated his prior testimony from his word processor. (R. 2540-41)

³⁷ In re the Investigation into the Reasonableness of the Rates and Charges of the Mountain States Telephone & Telegraph Company, Report and Order, Case No. 88-049-07, at 77 (Utah P.S.C. October 18, 1989). The Commission also noted that "the Division has not conducted an economic analysis" and that "the rapid employment of new technology is not always advantageous. Lacking firm and economic analysis we are unable to assess the benefits claim for accelerated replacement of switches." Id. at 76 (emphasis added). The Commission also indicated that "most new services can be supplied with the older central office switches." Id. A copy of the relevant portions of the Order in that case are attached as Addendum F.

Ironically, in Case No. 88-049-07, the Committee was adamantly opposed to an order requiring the upgrade of the electromechanical central offices. Its witness testified, among other things, that "[i]t would be foolish to suggest that rural areas have the same level of technology requirements as urban areas containing many companies which may require more sophisticated communications facilities." (R. 2222) The Committee witness also claimed that electromechanical switches had not outlived their useful life and they could still provide useful service. (R. 2225)

essential to customers or that the lack of them renders the electromechanical offices inadequate. In fact, the two major services cited by proponents of the upgrades are clearly irrelevant to the adequacy issue. The first group of services are custom calling features. While they are not available in electromechanical offices, they are, by the Commission's own characterization, non-essential services. In a 1988 order, the Commission characterized them as "non-essential, convenience services, the lack of which does not materially impact the basic service provided to end users." ³⁸ The second service is "equal access." Equal access is not a service regulated by the Utah Commission; rather, it is the capability of customers to gain access to interstate long distance carriers by dialing 1 plus the area code and telephone number (commonly called "1-plus" dialing). Mr. Fuller acknowledged that the interstate carriers have the right to order equal access in these offices and, when they do so, USWC would be compelled to upgrade the switch. (R. 2543-44) However, Mr. Fuller agreed that the interexchange carriers have not ordered equal access because they would need to financially support the upgrade. Id. Ironically, because equal access is an interstate issue and thus outside the Utah Commission's jurisdiction, the

³⁸In re Petition of the Mountain States Telephone & Telegraph Co. for Exemption from Regulation of Various Central Office Based Services, Report and Order, Case No. 86-049-17, at 9-10 (Utah P.S.C. June 25, 1988) The relevant portions of the Report and Order are attached as Addendum G.

Commission has disallowed equal access expenses for purposes of Utah ratemaking.³⁹ To exclude costs related to equal access in ratemaking and then use the lack of equal access as the basis for ordering central office upgrades is both inconsistent and unfair.

Perhaps the most important evidence presented below was the unrebutted testimony demonstrating that all essential services are available from electromechanical switches. As Mr. Dunkel acknowledged, basic exchange, extended area service, in-state long distance and access to interexchange carriers⁴⁰ are fully available from electromechanical offices. (R. 2211-13, 2230)

A recent decision in Oklahoma highlights the lack of substantial evidence in this case. In State v. Southwestern Bell, 825 P.2d 1305 (Okl. 1991), the Oklahoma Public Service Commission approved the expenditure of the utility's funds to upgrade 14 specific central offices listed on one of the Commission staff's exhibits. The Commission had found that the upgrades "will improve the quality of services . . . and increase the level of technology available to customers. . . ." Id.

³⁹ In re the Application of the Mountain States Telephone & Telegraph Company for an Increase in Rates and Associated Tariff Revisions, Report and Order, Case No. 85-049-02, at 62-63 (Utah P.S.C. December 31, 1985). The relevant portions of the Report and Order are attached hereto as Addendum H.

⁴⁰ AT&T can be accessed for interstate calls from electromechanical offices by using 1-plus dialing. (R. 2546) Other interstate long distance carriers can be accessed from electromechanical switches by using a dialing pattern requiring the input of a few additional digits. (Id.) Mr. Fuller indicated that dialling the extra digits is "not a substantial problem." (Id.) Thus, customers served by electromechanical offices do have convenient access to interexchange carriers.

at 1313. The problem in the case related to the fact that the particular list merely identified offices that “might” be considered. There was no evidence of the particular needs in each possible area of upgrade. On the basis of the record, the Oklahoma Supreme Court found that the order was not based on substantial evidence. The problem was that “the Commission’s order contained no reference to any specific information that could provide a basis for upgrading the listed central offices.” Id. While the factual context here is somewhat different, the essential problem is the same: there is no specific evidence relating to service inadequacy in each of the 41 central offices. The lack of such evidence as a matter of law compels the conclusion that the Commission’s inadequacy finding is not based on substantial evidence.

The Commission’s inadequacy finding fails for another reason. In Mulcahy v. Public Serv. Comm’n, 117 P.2d 298 (Utah 1941), the Utah Supreme Court, in dictum, articulated an economic test related to adequacy of service. In that case, the Court acknowledged the Commission’s authority to determine inadequacy of service based on several criteria. However, the Court’s ultimate conclusion was that the Commission could find service to be inadequate and order an upgrade “to the extent that the patronage received will justify the expense of rendering it.” Id. at 301. The Court thus explicitly adopted an economic test as a necessary element in decisions relating to adequacy of service. In its finding in this case, the Commission was unable to conclude that the upgrades were economical. (R. 5457) Thus, the record does not contain the essential finding that

upgrades are economical nor does it contain substantial evidence upon which such a finding could be made.

D. The Commission's rejection of the economic study provided by USWC was clear error.

As noted above, Mulcahy demonstrates that the economics of the central office upgrades is an essential issue to examine in addressing the adequacy of service issue. 117 P.2d at 301. Yet, on the economic issue, the Commission essentially entered a non-finding:

The Commission finds that the Company studies are not conclusive and may not include all the benefits identified on the record, and therefore the Commission cannot conclude that the proposed central office modernization is uneconomical.(R. 5457)

This finding is based on serious errors by the Commission.

The Commission's discussion of the "economic studies" in the order is based on a misreading of the evidence. In concluding that the upgrade of the central offices may be economical, the Commission indicates that the Company submitted three studies based on the CUCRIT⁴¹ methodology. (R. 5456) In fact, the Company presented only one study to the Commission: the CUCRIT study completed in February 1991 and filed as part of the surrebuttal testimony of Mr. Selander. (Selander Surrebuttal at 10-18. Exhibits 7SR.1-7SR.7, Addendum D) It is unrebutted that the other information characterized as "studies" by the Commission did not specifically study the 41 central offices at issue. As explained

⁴¹ CUCRIT is an acronym for Capital Utilization Criteria (R. 5456), which is the standard methodology used by USWC to evaluate the economics of capital deployment alternatives.

in depth by Mr. Williams, the information that the Commission characterized as “studies” was set forth in interrogatories which were based on an extremely general analysis of the economics of central office upgrades that did not focus on the 41 central offices. (R. 7024-27) At no time prior to the study presented by Mr. Selander were the 41 specific central offices ever studied in a specific CUCRIT study. (R. 7024-29) Thus, the only specific CUCRIT study of the offices in question was the one presented by Mr. Selander and described in detail by Mr. Williams. That study showed that upgrading to 41 central offices is clearly uneconomic. (USWC Exhibits 7SR.1-7SR.7, Addendum D)

Although that study was received into evidence, and was explained in great depth by the testimony of Mr. Williams, the Commission concluded that “[b]ecause this study was late filed, however, the parties could not adequately assess it. Therefore, the Commission cannot rely on it to make a finding.” (R. 5456) This is clear legal error. The CUCRIT study was provided as part of the surrebuttal testimony of Mr. Selander. It was filed as soon as it was finalized and in full compliance with the schedule outlined by the Commission. (R. 7027-29) It was filed in response to Mr. Dunkel’s erroneous characterization of the earlier data responses provided by the Company. (R. 6510-11, 6555-57, 7025-29) Thus, it was entirely appropriate that it be filed at that time and in that context. While counsel for the Committee initially reserved an objection to the admission of the study (R. 1668-69, 1781), that objection was never pursued. The CUCRIT study was received into evidence, as was the detailed testimony of Mr. Williams

explaining the background and nature of the study. (R. 1669, 2785)

The Commission's statement that the parties could not adequately assess the study is also clear error. The parties had every opportunity to pursue additional discovery and to examine the study in depth, but failed to do so. The study was provided on February 13; hearings did not commence until February 28. In the hearings, the Company offered to do whatever was necessary to allow the other parties to fully analyze the study. Counsel for USWC said this:

Maybe I should short-circuit some of this. To the extent the Committee feels a need to do further discovery and present further evidence, the Company has absolutely no problem with that in doing it at a later point if necessary. (R. 1778)

Thus, given the importance of this issue, the Company offered to do whatever was necessary to allow the parties to fully review the study.⁴² Chairman Stewart said the following to counsel for the Committee: "You have either got to petition for the opportunity to review these studies and take whatever time is necessary and/or just object to the receipt of these, which I will tell you we will probably not agree to." (R. 1780) Thereafter, counsel for the Committee interposed an objection to CUCRIT being part of the record, which was reserved for later discussion. (R.

⁴² At a later point in the hearing—during the cross-examination of Mr. Williams—counsel for USWC reaffirmed the offer:

Mr. Smith: Can I interject? I think we have already gone on the record as saying that to the extent the Committee needs additional time to do discovery and/or file additional testimony, the Company is not in any way wishing to preclude the Committee from so doing. So I'm not sure where this line of questions is going. (R. 2823-24)

1781) That objection was never raised again by the Committee. Neither the Committee nor any other party sought further review of the study.⁴³ Mr. Williams outlined in detail the basis for the CUCRIT study, the reason it was provided and how it differs from the prior interrogatory responses. This information was all received into evidence without objection. (R. 2785) As uncontradicted evidence in the case, the CUCRIT study should serve as the basis for a finding that the replacement of the 41 central offices is not economical.

In Jones v. California Packing Corp., 244 P.2d 640 (Utah 1952), the Utah Supreme Court held that the law does not invest the Industrial Commission with the "arbitrary power to disbelieve or disregard uncontradicted, competent, credible evidence," and that:

If the Commission could go so far as to refuse to believe such evidence, in the absence of anything to refute it, then it certainly would possess arbitrary powers with no effective review left available to the litigant.

Id. at 645. See also, DeVar v. Noble, 369 P.2d 290, 293 (Utah 1962) (arbitrary distortions of justice could occur if courts were permitted to ignore credible and uncontradicted evidence.) It was arbitrary and capricious for the Commission to ignore the CUCRIT study.

Furthermore, as the only study of the particular central offices in question, the CUCRIT study is the only substantial evidence on the record regarding the economics of the central office upgrades. Thus, the only substantial evidence in

⁴³ In response to a question asked by the Commission, both the Committee and Division stated that they were not going to respond to the study. (R. 2824) Indeed, the Division does not dispute the study's conclusion that the upgrades are uneconomic. (R. 5216, footnote 23; see also R. 2528-29)

the record demonstrates that the central office modernization proposal is indeed uneconomical. In concluding that the evidence is not conclusive and in failing to enter a finding that the upgrades were uneconomical, the Commission has therefore erroneously interpreted and applied the law, has failed to resolve all issues requiring resolution, and has acted arbitrarily and capriciously. Utah Code Ann. §§ 63-46b-16(4)(c),(d) & (h)(iv).⁴⁴

III. THE COMMISSION'S ORDER REQUIRING USWC TO DEPLOY FIBER OPTIC FACILITIES BETWEEN NEPHI AND ST. GEORGE AND TO DEPLOY A DISTANCE LEARNING NETWORK IS NOT BASED ON ADEQUATE SUBSIDIARY FINDINGS, IS NOT BASED ON SUBSTANTIAL EVIDENCE, AND IMPROPERLY ORDERS USWC TO MAKE INVESTMENTS WITHOUT PROPER NOTICE AND HEARING. IT SHOULD, THEREFORE, BE REVERSED.

A. The Commission's inadequacy finding relating to the fiber optic backbone and distance learning facilities is not supported by sufficient subsidiary findings.

In Section II.A, supra, USWC described the requirement that ultimate findings, like the Commission's "inadequacy" finding, be supported by "sufficient detail" and "critical subordinate findings." Milne, 720 P.2d 1378. The Commission's inadequacy finding appears to apply to the fiber backbone and distance learning facilities. Yet, there are absolutely no subsidiary findings to support the ultimate finding that existing services and facilities are inadequate. Thus, the inadequacy finding is insupportable and unreviewable and should not be allowed to stand.

⁴⁴ Under the Commission's view of CUCRIT, it would apparently be improper to base a finding on any new substantive evidence introduced in surrebuttal testimony. Such an approach is totally unfair and leads to the exclusion of pertinent evidence.

Likewise, in Section II.B on this Brief, USWC demonstrated that the Commission's failure to define "present day standards" and "present day service expectations" renders the inadequacy finding so vague as to be unreviewable. That same reasoning applies here as well.

B. The Commission's inadequacy finding regarding the fiber backbone and distance learning facilities is not based on substantial evidence.

The adequacy of the fiber backbone and distance learning facilities never became an issue below, since both the Division and Committee made no claim nor presented any evidence of inadequacy. Certainly there was evidence that these investments would create some general benefits in Utah, but there is a complete lack of evidence to support a finding that existing service and facilities are legally inadequate. Even the Commission acknowledged that "there is no formal analysis on the record concerning the economics of the fiber optic backbone and central office interties." (R. 5457) Thus, the economic test articulated in Mulcahy has not, as a matter of law, been met. 117 P.2d at 301.

Aside from general statements that these modernization proposals would be generally beneficial, there is no evidence to support an inadequacy finding. Furthermore, as a matter of law, the mere identification of qualitative differences between technologies does not lead necessarily to the conclusion that a regulatory agency can require the replacement of the older technology on inadequacy grounds.

C. Since no party requested that USWC be ordered to make the fiber backbone and distance learning investments in the absence of an acceptable incentive regulation plan, the Commission's order requiring USWC to make the investments is a denial of USWC's due process rights.

In the early stages of the proceeding below, the Commission became aware that some parties might take the position that USWC should be required to make some of the upgrades whether or not an incentive plan ever took effect. In an obvious attempt to make sure that the parties gave proper notice that modernization could be required by the order, the Commission, in its July 12, 1990 Scheduling Order, required that all parties file a "brief statement of position in this proceeding, including, specifically any design to argue for an ordered modernization plan in the absence of an incentive plan." (R. 3935, emphasis added) Several parties made such filings. (R. 3954-57, 3958-62, 4038-46, 4524-26, 4534-40, 4541-43) The Division and Committee made it clear that they would seek an order requiring the central office upgrades (R. 4525, 4542-43), but neither indicated that they would seek such an order for the fiber backbone or the distance learning proposals. Id. Only McCaw Cellular indicated that the Commission should order all aspects of the modernization plan, but conditioned such a requirement on a Commission finding that "the benefits of the programs exceed the costs . . ." (R. 4536) The McCaw filing proved to be irrelevant since McCaw, prior to hearing, withdrew its testimony. (R. 5073-75) As noted in the Statement of Facts, the Committee and Division were not neutral on the question of an order requiring fiber optic and distance learning upgrades - in their testimony they actively opposed such an order. Thus, at the time of the hearings, no party had

filed testimony or had otherwise notified USWC that it would seek such an order. It is, therefore, no surprise that there was no evidence presented on the issue of service adequacy relating to the fiber backbone and distance learning facilities – no one in the case perceived it to be an issue.

The Commission's order requiring the deployment of facilities that no party proposed violates the fundamental constitutional principle of due process that tribunal may not grant relief that was not requested. In Combe v. Warren's Family Drive-Inns, 680 P.2d 733 (Utah 1984), the Utah Supreme Court stated:

In law or in equity, a judgment must be responsive to the issues framed by the pleadings, and a trial court has no authority to render a decision on issues not presented for determination. Any findings rendered outside the issue are a nullity.

Id. at 736. Accord, Cornia v. Cornia, 546 P.2d 890, 893 (Utah 1976) ("liberality in procedure . . . does not authorize granting of relief on issues neither raised nor tried.").

That due process requires adequate notice of the relief requested and ultimately granted is inherent in the constitutional right of due process under the Fifth and Fourteenth Amendments to the U. S. Constitution and Article 1, Section 7 of the Utah Constitution.⁴⁵ In Morgan v. United States, 304 U.S. 1 (1938), the United States Supreme Court described the right this way:

But a 'full hearing'—a fair and open hearing--requires more than that. The right to as hearing embraces not only the right to present evidence, but also a reasonable opportunity to know the claims of the opposing party and to meet them. The right to submit argument implies the opportunity, otherwise the right may be barren one.

⁴⁵ U.S. Const., Amendment V & XIV; Utah Const., Article 1, § 7.

Id. at 18 (emphasis added). The courts of Utah recognize these same principles. In Nelson v. Jacobsen, 669 P.2d 1207 (Utah 1983), the Utah Supreme Court stated the basic principles relating to adequacy of notice and the opportunity to respond:

Timely and adequate notice and an opportunity to be heard in a meaningful way are the very heart of procedural fairness.

...

To satisfy an essential requirement of procedural due process, a 'hearing' must be prefaced by timely notice which adequately informs the parties of the specific issues they must prepare to meet. . . . In cases where the notice is ambiguous or misleading, courts have found a denial of due process. . . .

"Due process" is not a technical concept that can be reduced to a formula with a fixed content unrelated to time, place, and circumstances. Rather, the demands of due process rest in the concept of basic fairness of procedure and demand a procedure appropriate to the case and just to the parties involved.

Id. at 1212-13 (citations and quotation marks omitted, emphasis added). See also Tripp v. Vaughn, 746 P.2d 794, 796 (Utah App. 1987) ("The notice must adequately inform the parties of the specific issues they must prepare to meet."). Since there was no request for an order requiring USWC to make the fiber optic and distance learning investments, and therefore no notice of a request for such relief, the order is a clear and direct violation of the due process rights of USWC and must be reversed.

CONCLUSION

It is clear from the foregoing legal arguments that significant portions of the Commission's order cannot be sustained on appeal. Therefore, USWC respectfully requests that the Court:

1. Reverse the Commission's refusal to consider the normalization adjustments proposed by USWC, remand the matter to the Commission with the direction to consider those adjustments, and to require that, to the extent the adjustments are accepted, USWC be allowed to recover from ratepayers the revenues it should have received had the Commission correctly interpreted and applied the Stipulation.
2. Reverse the Commission's decision requiring USWC (1) to replace the 41 electromechanical central offices, (2) to place the fiber backbone facilities, and (3) to place the distance learning facilities.

Respectfully submitted this 23rd day of November, 1992.

A handwritten signature in black ink, appearing to read "Ted D. Smith", written over a horizontal line.

Ted D. Smith
Attorney for Appellant
U S WEST Communications, Inc.

CERTIFICATE OF SERVICE

I hereby certify that on the 23rd ^{November} ~~October~~, 1992, I caused four (4) copies of the foregoing **BRIEF OF APPELLANT U S WEST COMMUNICATIONS, INC.** to be mailed, first class mail, postage prepaid, to the following:

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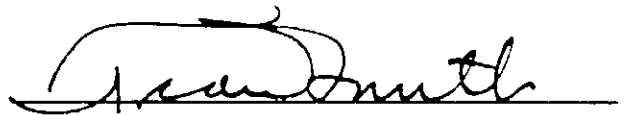
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ADDENDUM A

EXCERPTS FROM THE
REPORT AND ORDER OF THE
UTAH PUBLIC SERVICE COMMISSION

JUNE 19, 1991

CONSOLIDATED DOCKET NOS. 90-049-03 & 06

DOCKETED

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Application)
of US WEST COMMUNICATIONS for)
Approval of an Incentive Regulation)
Plan.)

DOCKET NO. 90-049-03

REPORT AND ORDER

In the Matter of the Investigation)
into the Reasonableness of the)
Rates and Charges of US WEST)
COMMUNICATIONS.)

DOCKET NO. 90-049-06

ISSUED: June 19, 1991

SHORT TITLE

1990 General Rate Case

SYNOPSIS

The Commission herein orders a reduction in revenue requirement of \$19,799,000. The reduction is based on a stipulation by the parties on all issues except depreciation expense and cost of capital, which is set by the Commission at 12.2 percent rate of return on common equity and 10.93 percent rate of return on investment. Revenue requirement reductions ordered in this docket, the sum of two interim reductions and this final one, total \$38,748,000. In addition, the Commission adopts a proposal to invest in central office and transport plant and equipment to modernize and upgrade the network. The Commission also formulates an "incentive regulation" plan which, if implemented, would permit the Company to retain a share of excess earnings, if any, over the allowed rate of return, as an incentive to promote more efficient utility operations.

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I. PROCEDURAL HISTORY

On March 2, 1990, US WEST Communications (USWC or the Company) filed an application with the Commission seeking approval of an incentive regulation plan. Docket No. 90-049-03 was assigned to the case. As part of the application, USWC provided a general description of its proposed plan, which contained both incentive regulation and network modernization proposals. On March 16, 1990, the Committee of Consumer Services (Committee) filed a Motion to Dismiss Application and Strike Docket on the ground that Senate Bill 115, the legislation that enacted Utah Code Ann. Section 54-4-4.1 (1991), had not yet become law. On March 26, 1990, USWC filed its detailed Utah Incentive Regulation Plan.

On March 28, 1990, the Division of Public Utilities (Division) filed a Petition in Docket No. 90-049-06 seeking an investigation into the reasonableness of the rates and charges of USWC and requesting a hearing to consider an interim rate reduction of \$5.7 million.

On April 27, 1990, the Committee withdrew its Motion to Dismiss when USWC agreed that its application be deemed to have been refiled on April 27, 1990. In its Order of May 10, 1990, the Commission ruled that USWC's application and other pleadings relating to incentive regulation would be deemed to have been refiled as of April 27, 1990 without the necessity of actually refiling them. In the same order, the Commission ordered that Docket Nos. 90-049-03 and 90-049-06 be "consolidated for purposes of hearing only," and

established a schedule for filing of testimony and for hearings. The Commission required that analyses of both the incentive and the modernization plans consider the current definition of "universal service" as well as what would be required when the term of a plan ended. In late April 1990, the Division and the Committee filed testimony in support of their requests for an interim decrease. On May 1, 1990, the Committee filed a motion requesting that the Commission reduce rates on an interim basis by \$16 million. On May 18, 1990, USWC filed responsive testimony regarding the proposed interim rate decrease. The Division filed supplemental testimony on May 18 and May 23, 1990, increasing its requested interim decrease to \$8.6 million. Hearings were held on May 24-25, 1990. Following the hearings, various parties filed briefs summarizing their positions regarding the proposed interim rate decrease. On June 22, 1990, the Commission ordered an interim rate decrease of \$10.65 million, based on a 1989 test year, 11.8 percent return on equity, and adjustments consistent with those ordered in Docket No. 88-049-07. The Commission also determined that the standards for interim rate decreases and increases need not be the same.

On June 29, 1990, USWC filed its direct testimony on incentive regulation issues, as well as amendments to its proposed Utah Incentive Regulation Plan. On July 12, 1990, the Commission issued its order amending the schedule. On July 20, 1990, parties (other than USWC) filed position statements on incentive regulation issues. On August 14, 1990, the Commission issued its Second Amended Scheduling Order revising some of the filing and hearing dates. On

August 27, 1990, various parties filed their preliminary revenue requirement calculations. On September 8-9, 1990, the Second Amended Scheduling Order was published in the Salt Lake Tribune and the Deseret News. In early October 1990, various parties filed testimony on rate of return and capital structure issues.

On October 24, 1990, all parties filed testimony in response to USWC's proposed incentive regulation plan. On October 30, 1990, USWC, the Division, the Committee, and AT&T entered a Stipulation and Joint Motion on Revenue Requirement Issues, resolving most revenue requirement issues, and calling for a further interim reduction of \$8.238 million to be implemented January 1, 1991. On October 31, 1990, James L. Barker, representing himself and six other intervenors, filed a Request for Declaratory Order challenging the constitutionality of 54-4-4.1, the statute that enables the Commission to adopt earnings sharing plans like the one proposed by USWC. On November 1, 1990, the Commission issued its Third Amended Scheduling Order. On November 23, 1990, the Commission issued its Fourth Amended Scheduling Order in which it ordered parties to consider the effects of demand for service on depreciation, and stated that the determination of revenue requirement must address the persistence of overearnings. In addition, the Commission ordered that the interim rate reduction be spread on an equal percentage basis to residence and business local exchange services, toll, and switched access, excluding nonrecurring charges, and stated the Commission's determination of its authority to order investments to upgrade the system. On November 26, 1990, the parties filed rebuttal

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testimony on rate of return and capital structure issues. On December 4, 1990, pursuant to the request of the Company, the Commission issued a Revised Public Notice of Hearing, which was published in the Salt Lake Tribune and the Deseret News on December 8-19, 1990, and which was mailed directly to all persons and entities who had filed letters with the Commission indicating an interest in incentive regulation and network modernization issues. On December 8, 1990, the parties filed surrebuttal testimony on rate of return and capital structure issues. On December 17-19, 1990, the Commission held hearings on the Stipulation and Joint Motion on Revenue Requirement and on rate of return and capital structure issues. By order issued January 3, 1991, the Commission approved the Stipulation pursuant to its terms. On January 11, 1991, the parties filed briefs on rate of return and capital structure issues. On January 16, 1991, all parties filed rebuttal testimony on incentive regulation issues. On January 18, 1991, the parties filed testimony on depreciation represcription issues. Also on January 18, 1991, several parties filed briefs and motions responding to Mr. Barker's Request for Declaratory Order. On January 22, 1991, the parties filed direct testimony on rate design issues. In late January and early February 1991, various witnesses filed additional testimony on depreciation represcription issues. The Commission held a hearing on February 8, 1991 on depreciation represcription. Also on February 8, 1991, Mr. Barker filed a Reply Memorandum regarding the constitutional issues. On February 15, 1991, the parties filed surrebuttal testimony on incentive regulation issues and rebuttal

testimony on rate design issues. On February 22, 1991, the Commission issued an order dismissing Mr. Barker's Request for Declaratory Order. Hearings on incentive regulation and rate design issues commenced on February 28, 1991 and concluded on March 13, 1991.

On April 19, 1991, USWC, the Division and the Committee filed position statements regarding disputed issues relating to the Stipulation and Joint Motion on Revenue Requirement Issues. On April 26, 1991, the same parties filed responsive position statements. On May 1, 1991, USWC moved that the Commission accept the position statements as evidence in this proceeding and sought oral argument. On May 15, 1991, USWC, the Division and the Committee presented oral argument on the disputed issues relating to the Stipulation and the position statements were accepted as evidence in this proceeding.

II. DISCUSSION, FINDINGS, AND CONCLUSIONS WITH RESPECT TO REVENUE REQUIREMENT

A. STIPULATION

On October 30, 1990, the parties entered into a Stipulation that was intended to resolve all revenue requirement issues except depreciation and cost of capital, which were reserved for later hearing. Following hearings on December 17th, the Commission adopted the Stipulation by order issued January 3, 1991.

The October Stipulation was based on the first six months of 1990 actual results of intrastate operations then available and the Company's budget estimates for the calendar year 1990.

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Attached to the Stipulation was a Joint Exhibit in which 32 adjustments to actual results were identified. The value of 23 of the adjustments were to be held fixed, including the June 22, 1990 interim rate reduction, and the value of the remaining nine adjustments were to be updated when actuals for all 12 months of 1990 became known. The intent of the signatory parties to rely on the Stipulation as crafted and to exclude consideration of further adjustments is made clear in paragraphs six and seven of the Stipulation.

The Stipulation is a negotiated settlement of revenue requirement issues, as distinct from each party advancing its own interest through discovery and hearing, in an adversarial way, on every single issue. Negotiation is a process of compromise in the interest of reaching an end result that each party is able to accept. The Commission has criticized this process of bargaining and compromise before, because it leaves the Commission unaware of important details. The Commission knows only outcomes. In addition, and perhaps most importantly, some issues have been "decided" in the course of the negotiations without having been brought to the Commission's attention. Therefore, the Commission has been reluctant to accept stipulations in recent major cases, and, where stipulation seemed the prudent course, has sought to confine them to purely technical as distinct from policy issues.

In the current docket, stipulation was entertained as the reasonable course in order to free up Company and regulatory resources to deal with the Company's incentive and modernization

proposals. Also, it seemed revenue requirement issues, according to the parties, could be resolved in conformance with Commission decisions rendered in the previous, recently concluded Docket No. 88-049-07. Since the issues were not to be reargued, the policy aspect was removed, and resolution would be on technical grounds.

It is in this context that, later in the docket proceedings, parties began to argue the meaning of the Stipulation's limitation on updates and adjustments of test year data. USWC proposed four new adjustments to test year data, on issues the other signatory parties had not seen at the time the Stipulation was signed and which had the effect of increasing revenue requirement. The Division then sought to update several of the 23 adjustments which the Stipulation said could not be updated and which had the effect of decreasing revenue requirement. The Committee argued that the plain meaning of the Stipulation prevented either the introduction of new adjustments or the updating of fixed adjustments, and urged the Commission to reject them both.

The Commission could not have been presented a more penetrating example of the problematic nature of stipulations. Here, signatory parties could not agree what their own words meant, and seized this dispute as an opportunity to advance their own interests on what otherwise might have been reasonable grounds. USWC argued its proposed new adjustments were of the sort routinely permitted in the normal fashioning of a test year. With the full 12 months of 1990 actual results of operations information in hand, the Division

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argued the superiority of these "actuals" to the budget information upon which the Stipulation was based.

When the Commission accepted the Stipulation on January 3, 1991, the nature of the document as a compromise based on the best information then available to the parties was clearly understood. That each party must have given up something in signing the Stipulation, and might on some issues have argued differently if given the chance in an adversarial proceeding, goes without saying; that is the very purpose of negotiation in a settlement conference. It is what is meant by stipulation. Parties cannot now come back to the Commission and attempt to redefine things to their own advantage. To do so places the Commission at an unacceptable disadvantage and severely compromises case proceedings. The record does not contain full examination of contested issues. The Division has not audited the 1990 information and neither the Division nor the Committee can state what, except for the agreement reached in the Stipulation itself, the test year would ideally be.

There has also been some discussion about what the parties could, did, or should have understood was contemplated by the Stipulation. At this point in time, all that is important is what the Commission understood to be stipulated to by the parties at the time it accepted the Stipulation. None of the adjustments now argued for by USWC or the Division were considered open issues by the Commission. On this basis, the Commission has two choices. The Stipulation can be accepted without alteration except as specifically permitted by its terms, or the case record can be reopened for

receipt of further information intended to redefine the test year. Reopening the record is not acceptable. To do so would be tantamount to beginning the revenue requirement determination anew. There is no doubt that each moment's delay in reducing rates costs ratepayers money. This the Commission cannot countenance. Therefore, the Commission concludes the Stipulation must be accepted essentially unaltered. Parties are, as always, free to bring a new action to further examine rates as soon as this order is final.

The Commission finds that the new adjustments proposed by the Company are not permitted by the terms of the Stipulation and are therefore rejected. The Commission finds that the updates proposed by the Division are not permitted by the terms of the Stipulation and are likewise rejected.

There exists one remaining dispute regarding the interpretation of the Stipulation, that being the treatment of the June interim rate reduction. On June 22, 1990, the Commission ordered that rates be reduced to achieve a revenue reduction of \$10,655,000 pending a final order establishing permanent rates in this proceeding. As implemented the interim reduction totalled \$10,711,000 effective June 22, 1990, for local exchange service, July 1, 1990, for 800 and OutWATS services, and July 18, 1990, for message toll and switched access services. In the Stipulation the parties have agreed to properly annualize and normalize 1990 actual revenues to reflect the realized \$10,711,000 revenue decrease on a prospective annual basis.

What is in dispute is the method by which the interim reduction is to be annualized. The Company interpreted the Stipulation to mean that the total \$10.7 million be removed from actual 1990 revenues as if the reduction had been in place for the entire year as shown in the Joint Exhibit attached to the Stipulation. The Division and the Committee interpreted the Stipulation to mean that the method of annualization should reflect the mid-year timing of the reduction and that the \$10.7 million shown in the Joint Exhibit was to illustrate the parties' agreement to the total reduction to be considered as the basis for annualization. In order to fully reflect the realized \$10,711,000 revenue reduction on a prospective, annualized basis as agreed to by the parties, the Commission finds that actual 1990 revenues need to be reduced by \$5,080,000 to account for the mid-year timing of the interim reduction and thereby remove the impact of the higher rates in effect only during the first half of 1990.

B. DEPRECIATION

On November 23, 1990, USWC submitted its triennial depreciation study to both the Federal Communications Commission (FCC) and this Commission. This study proposed changes in the projection-lives and future-net-salvage parameters previously approved by the Commission in 1988. In conjunction with the rate case and the Incentive Regulation Plan, the Commission requested that the Division review the study and report to the Commission with recommendations. Following its review of the study, the Division

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section. All of these changes will be displayed in a final table to be attached to this Report and Order.

IV. NETWORK MODERNIZATION

A. INTRODUCTION

In this case the Company has submitted a proposal for modernization of its network in conjunction with its incentive regulation plan. According to Company witness Phillip S. Selander, the proposed modernization investments will be "a beginning or seed for the network of the future [and] they will give us the fiber optic and digital building blocks from which we can expand." The modernization plan would accelerate the installation of new central office switching and interoffice facilities in order to support the wide variety of capabilities and services that the network of the future may require. Thus, Company witnesses testified that the modernization plan is an important investment in Utah's future.

B. DESCRIPTION OF THE PLAN

The modernization plan, as presented by the Company, is primarily aimed at upgrading rural central offices and laying a fiber optic network to facilitate telecommunications for educational, governmental and hospital use as well as for residential and business customers. This would permit high-speed, high-capacity data transfer and accommodate two-way video transmissions in support, for example, of "distance learning." The upgrade would improve service for rural customers, the Company stated.

The modernization plan the Company originally filed on March 2, 1990, called for \$103 million in additional capital to be invested in Utah. \$52.46 million of the investment is for the replacement of 46 electro-mechanical central office switching equipment with digital switching equipment and the remaining \$51.67 million is for new interexchange fiber optic cable. When in place, according to the Company, high capacity transmission would exist from Brigham City to Cedar City, with digital radio extensions to Logan, Price, St. George and Vernal. The plan also included the construction of local fiber networks to connect central offices to universities, colleges and high schools. The Company stated that all projects would be completed within 54 months from the date of the Commission's order in this docket.

The Company's proposed plan was revised in response to testimony by the Division and the Committee, and by the Company's conclusion that five of the central offices in the original plan and transmission from Brigham City to Logan would hit "hard triggers", i.e., growth would exhaust capacity, requiring an immediate upgrade in order to maintain service. The Company's witnesses Robert C. Fuehr, Kirk R. Nelson, and Phillip S. Selander, in later filings and oral testimony, described the Company's revised modernization proposal. The revised plan proposed an upgrade to digital technology of the 41 remaining electro-mechanical central offices. The central office upgrade and facility augmentations needed to support such upgrades to digital technology were estimated to cost \$36.35 million on a total state basis and \$25.76 million on an intrastate basis, over a five-year period.

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The second part of the revised plan is an expansion of the fiber optic and digital infrastructure "backbone" so that it runs from Logan to St. George, with upgraded digital microwave extensions to Vernal and Price. The Company consented to the Division's recommendation that the fiber optic extensions in support of higher education and distance learning, i.e. local fiber optic loops from central offices to every college, university and high school, would be installed only when economical. The estimated capital cost of the fiber extension is \$21.5 million. The commitment to lay fiber cable to all colleges, universities and high schools and school district offices when economical requires the investment of \$33.88 million in discretionary capital.

C. BENEFITS OF MODERNIZATION

All parties to this case agree that there are substantial benefits to be gained from modernization in general and the Company's proposed modernization plan in particular. Mr. Fuehr testified that "communications will become an even more critical link than it is today in the economic well-being and development of a highly mobile and technical society.... Telecommunications will play [a role] in enhancing the global competitiveness of Utah businesses." Company witness Dr. Davidson testified that in order to remain economically competitive, states would have to upgrade their telecommunication networks. He alerted the Commission to the consequences of inadequate investments in new technology: "Without modernization to provide higher quality, lower cost and advanced services, the gap between public and private offerings will widen, sophisticated users will shift increasingly to private networks and the remaining users

will find it difficult to secure basic and enhanced services at reasonable rates.... The ultimate impact of inadequate public telecommunications capacity on local economic and social conditions remains to be seen, but it could place selected regions and segments of society at a distinct disadvantage."

Company witness Selander stated that educational needs alone technically would justify the proposed enhancements, but when combined with government and research needs, the modernization project is even more economically feasible. The enhancements in the digital infrastructure would allow the system to carry a wider variety and greater quantity of traffic more economically. According to the Company, its new capabilities would include distance learning, a higher education library network, and a research network connecting universities, colleges and businesses to a centrally-located super computer. Utah State University's ComNet and the state government's digital communications requirements could be met. The Company testified that the increase in telecommunications services would promote economic development in general and rural development in particular.

A number of public witnesses testified in favor of fiber optic extensions to colleges, universities and high schools in support of distance learning. Mr. Steven Hess, Director of the Utah Educational Network, testified that it was his organization's goal to extend its distance learning service to every rural high school and applied technology center in need of the service, within the next five years. He further testified that the extension of fiber to those facilities would provide the capacity needed for such expansion. Dr. Bartell C. Jensen, Vice President for Research at Utah State University (USU)

and Dr. Glenn R. Wilde, Executive Director of the Merrill Library and Electronic Distance Education at USU, testified that the communications network proposed by U S WEST would provide the capabilities of two-way interactive video at community sites, schools and colleges and universities in the state. They further testified that the proposed U S WEST network would provide a critical and needed backbone service to make a statewide educational and training system workable. Mr. Will Gardner of BYU, and Chairman of UTAHNET, a Task force chartered by the Utah State Advisory Council for Science and Technology to study the needs for high capacity telecommunications in Utah, testified that upgrading the telecommunications infrastructure to reach schools (especially in the rural areas) with interactive television capabilities would be the single most effective way to upgrade the educational posture of the entire state.

In addition, the Commission has received many letters from educators, community leaders and concerned citizens in support of the modernization proposal.

The Company, the Division and the Committee offered testimony that the proposed central office upgrades would make enhanced services and capabilities available to all USWC's customers, including rural customers presently unable to obtain such services as equal access to interexchange carriers and such custom calling features as call waiting, call forwarding, speed calling, and 3-way calling. In addition, the upgrades will provide for more accurate and clearer transmission of voice and data. Further, the upgrade will allow the offering of additional CLASS services when the Company begins to market them in the state.

The Commission finds that the central office upgrades will provide more accurate processing of dialed digits, faster touch tone services, faster call completion, clearer conversations and more accurate data transmissions. The Commission further finds that the modernization plan will enable USWC to provide new services that are not currently available in Utah. In addition, the Commission finds that the proposed investments would be of benefit to and would meet a wide variety of residential, business, educational, governmental and research needs, and concludes that the Company's proposed modernization program is clearly in the public interest.

D. RISKS OF MODERNIZATION

The Company maintained that the proposed investments contained in its modernization plan, and in particular the investments in upgrading central offices, were discretionary and would not be made in a business-as-usual environment. These investments, although yielding benefits to the state and its citizens, might get subordinated to other investment opportunities. The Company maintained that modernization investments, while providing net benefits, are riskier in that the expected earnings received by USWC are less than the expected earnings on other possible investments. The Company claimed that only the opportunity to earn higher profits through a change in regulatory form would induce it to carry the additional risks of modernization investments. USWC maintained that the modernization plan is a good faith effort to demonstrate its intent to further its investment in Utah. The Company believes that by making investments that have high social benefits but low internal

rates of return to the Company, it demonstrates its commitment to the public interest.

The Company also argued that discretionary modernization investments can be risky in that they may not be incorporated into rate base. If the regulatory body determines that an investment is not prudent, then the shareholder must bear its cost. The Division pointed out that in the recent past there has not been a case where a major USWC investment had been excluded from rate base and, therefore, the risk to the Company is minimal. It contended that an understanding of this Commission's regulatory treatment of the Company's past investments is necessary to any analysis of the regulatory risk of a particular future investment.

The Company asserts that it may turn out that the demand for high capacity transmission is limited at present causing the revenues generated to be insufficient to fully cover costs. But the testimony of the other major parties was to the effect that if the investment is included in rate base, rates will be set to recover the costs, and thus the Company will be protected.

Both the Division and the Committee testified that most of the central offices included in the modernization plan are scheduled to be replaced by 1996 in the Company's business-as-usual budget. Thus, the plan would accelerate already planned investment by just a few years.

The Commission finds there is substantial evidence on the record that the modernization investments will benefit Utah in the near and long term future and are, therefore, a prudent risk for ratepayers.

There was considerable testimony on the record by the Division and the Committee asserting that depreciation policies adopted by the Commission have provided the Company the opportunity for rapid recovery of investment. The Company therefore has the ability to respond to rapid changes in technological innovation and emerging new, specialized customer demands without undue rate shocks to the general body of ratepayers. The Commission finds that the Commission has protected the Company's recovery of investment by adopting liberal depreciation policies.

Company witness Dr. William H. Davidson warned the Commission that it should not prescribe by order additional investment in the state of Utah. Any such effort could be circumvented by a reduction of investment elsewhere in the state. This could degenerate, he argued, into a situation where the Commission is forced to micro-manage the Company and thus assume responsibility for the investment decisions of the Company. The Commission ought not to have any desire for such a role. According to Dr. Davidson, the principal way to increase investment in Utah is to increase the rate of return on investments. He testified that the incentive plan is the most efficient way to raise the rate of return.

The Commission admonishes the Company against compensatory decreases in investment in other areas. There is evidence on the record of the Company's planned investment for the state absent an incentive plan. The Commission does not wish to see any gross deviations from those plans. USWC's investments in the state must insure a high quality of service as determined by this Commission. Appropriate regulatory measures will be taken to insure such quality of service. USWC possesses a certificate of convenience and

necessity and franchises to provide essential public services throughout its service territory. The Commission finds that the Company has the obligation to provide such services, determined by this Commission, so long as it holds that authority.

The Company also contended that its modernization plan in conjunction with the incentive plan increases its risk exposure. Such risk raises shareholders' required rate of return and therefore should be reflected in the incentive plan. Thus, the Company argued in favor of a gap between the authorized rate of return and that above which a sharing of earnings with ratepayers would commence. The Company maintained that it is at risk if the cost of capital increases. The Commission finds that such risk is attendant to the incentive plan alone and should not affect any decision on modernization. The Commission finds that neither the Company nor the ratepayer bears inordinate risk in modernizing the remaining electro-mechanical central offices, extending its digital "backbone" infrastructure, or the fiber optic extensions as contemplated by the Company's proposed modernization plan.

E. COMMISSION AUTHORITY

The Company has persuasively argued that the benefits of rural upgrade and modernization are substantial and those benefits are detailed herein and throughout this record. All parties are agreed that the public interest would be served by the modernization program proposed by the Company. At issue is the Company's insistence that the program is uneconomical without a change in regulatory framework as it has proposed in its incentive plan and that the Commission is

without authority to order modernization unless the Commission finds that the upgrades will be economical.

As clearly stated above, we do not agree that we must make such a finding. Nonetheless, we are of the view that the program may on the whole be economical. The Company submitted three studies on the economics of modernizing the central offices using its Capital Utilization Criteria (CUCRIT) model. The first study was submitted in response to the Committee's interrogatories concerning modernization. This response used data from a 1988 study on the then 54 remaining electro-mechanical central offices in the state. The study narrowed its analysis to the originally proposed 46 offices and concluded that modernization of these offices as a whole was uneconomic. However, as pointed out in the Committee's testimony, the study excluded the additional revenues that would be generated by the new services available from the upgraded offices. The Company updated this study by including these additional revenues and excluding five central offices that had reached "hard triggers". This study indicated that three of the central office upgrades were economical, 19 were marginally economical and 19 were uneconomical. Taken as a complete package, the investment was deemed by the Company to be marginally economical.

Mr. Fuehr ordered a new CUCRIT study in December of 1990 and late-filed with the Commission on February 13, 1991. This study examined the economics of the 41 central offices that were included in the revised modernization plan. It concluded that such modernization was uneconomic. Because this study was late filed, however, the parties could not adequately assess it. Therefore, the Commission cannot rely on it to make a finding. In addition, there

is no formal analysis on the record concerning the economics of the fiber optic backbone and central office interties.

In sum, the evidence purporting to show the Commission that the modernization program is uneconomical is not persuasive. The Commission finds that the Company's studies are not conclusive and may not include all of the benefits identified on the record, and therefore the Commission cannot conclude that the proposed central office modernization is uneconomical.

The Company cites two cases, the Mulcahy case (Mulcahy v. PSC, 117 P.2d 298, 1941) and the Lifeline case (Mountain States Telephone v. PSC, 1988) in support of its position that the Commission cannot order the Company to make expenditures which are uneconomical. Neither of those cases is convincing. The Mulcahy case is a trucking case in which the Commission was required to determine whether or not to grant a trucking company an operating certificate over opposition from an already certificated carrier for the same territory. In dictum the Court discusses the criteria for determining whether public convenience dictates that a new carrier be certificated in the territory and refers to the need to have the patronage for the service to justify the expense of rendering the service. That fact situation is completely different from the one facing the Commission here. In this case the Commission is considering the advisability of having a regulated utility upgrade its service. There is no debating whether or not another phone company should be granted a certificate in USWC's existing service territory. Clearly, the criteria for the entry of a competitor into an existing utility's service territory would be different and more stringent than the criteria for requiring an existing utility to upgrade its service. It is not unreasonable

in the Mulcahy case, as opposed to this one, that the Court should require that the would-be competitor's rates be cost-justified so as not to be predatory.

The Lifeline case stands for the proposition that the Commission lacks a specific delegation of legislative authority to have the customers of one utility in this state bear some of the cost of a program for the customers of another utility in this state.

This present case is not dealing with separate utilities--it is dealing only with USWC. The issue is whether or not the Company should be required to provide upgraded service for its own customers, not the customers of another utility. In the Lifeline case the Court determined that the Commission lacked a legislative delegation of authority to direct the Company to surcharge its customers for a statewide pool of Lifeline program funds that would be used for the customers of all phone companies. That has nothing to do with the Commission's authority to order an upgrade in the utility service offered by a utility to its customers. These are apple and orange issues.

There are multiple statutory references to the Commission's authority to require adequate service which supplement the Commission's general jurisdictional grant at 54-4-1:

The commission is hereby vested with power and jurisdiction to supervise and regulate every public utility in this state, and to supervise all of the business of every such public utility in this state, and to do all things, whether herein specifically designated or in addition thereto, which are necessary or convenient in the exercise of such power and jurisdiction.

The first of these is 54-4-7, which is a clear and plain statement of the Commission's authority to regulate and supervise the

services and commodities provided by utilities and order changes where present services are no longer adequate.

Whenever the commission shall find, after a hearing, that the rules, regulations, practices, equipment, appliances, facilities, or service of any public utility, or the methods of manufacture, distribution, transmission, storage or supply employed by it, are unjust, unreasonable, unsafe, improper, inadequate or insufficient, the commission shall determine the just, reasonable, safe, proper, adequate or sufficient rules, regulations, practices, equipment, appliances, facilities, service or methods to be observed, furnished, constructed, enforced or employed, and shall fix the same by its order, rule or regulation.

Section 54-4-8 is in the same vein.

Whenever the commission shall find that additions, extensions, repairs or improvements to or changes in the existing plant, equipment, apparatus, facilities or other physical property of any public utility or of any two or more public utilities ought reasonably to be made, or that a new structure or structures ought to be erected to promote the security or convenience of its employees or the public or in any way to secure adequate service or facilities, the commission shall make and serve an order directing that such additions, extensions, repairs, improvements or changes be made or such structure or structures be erected in the manner and within the time specified in said order.

Section 54-8b-11 charges the Commission with making available to customers throughout the state high-quality, universal telecommunications services. Section 54-3-1 requires that utilities provide equipment and service which promotes the safety, health, comfort and convenience of its customers.

The adequacy and convenience of service and equipment can change over time. Operator-switched calls and multi-party lines were once considered adequate; obviously, they no longer are. The Company itself has admitted on this record that the simple ability to complete a call in today's environment does not constitute adequate service. The Commission finds that service to certain customer areas

is not adequate by present day standards and that the modernization program is necessary at this time to provide all customers in this state with adequate and convenient service. It is, therefore, in the public interest. We conclude that it is for this Commission to determine what is necessary and convenient in the way of utility services, require the utility to provide it and allow that provider an opportunity to earn a fair return on its investment.

F. SUMMARY

The Commission recognizes that telecommunications provides beneficial externalities. A modern telecommunications infrastructure permits the efficient and economical flow of information, to the benefit of consumers of all sorts. As a result, it also may promote economic development.

Prudent and properly timed modernization is an important requirement facing the telecommunications industry. Therefore, it is a necessary element of good regulatory policy to promote economic and timely modernization. This Commission will encourage timely, socially beneficial investments, and will allocate corresponding costs fairly and equitably.

The Commission has found that the public interest requires the Company to undertake its modernization plan, whether or not its proposed incentive plan is approved. USWC will have the opportunity to earn its allowed rate of return on the proposed modernization investments and, therefore, will be compensated for the risk of such investment.

The Company must not provide discretionary modernization investment at the expense of investments otherwise undertaken to

maintain high quality service for the general body of ratepayers, however. The Company's investments in the state must insure high quality service, as determined by this Commission. Appropriate regulatory measures will be taken to insure that this occurs.

The Commission finds that existing services are no longer adequate and concludes that the modernization plan is justified in that it brings telecommunications in Utah in line with present day service expectations. Therefore, it is appropriate to order the Company to provide central office upgrades estimated to cost \$36.35 million and fiber-optic extensions so that the fiber optic infrastructure extends from Logan to St. George, with digital microwave extensions to Vernal and Price, at an estimated cost of \$21.5 million. These figures are represented by the Company to be the costs associated with these modernization investments. The Commission is ordering the modernization of the network, not the Company's estimated costs. The investments will be subject to the normal prudence reviews in future rate cases. As previously noted, the Commission, in the past, has not found the Company's investments to be unreasonable or excluded them from rate base.

The Division and the Company supported the proposed extension of fiber to colleges, universities and high schools only where deemed to be economically justified. As noted above, originally the Company proposed that the estimated \$33.88 million to extend fiber to such institutions would be a part of the overall modernization plan. The Commission is satisfied by the testimony on the record, including that of the public witnesses, as to the benefits of such extension. The Commission finds that fiber to the colleges, universities and high schools in the Company's territory is in the public interest and

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ought not be purely discretionary. The Commission further finds that the Company must work with the Division and the various interested educational interests in the state to devise a program entailing the investment for extending fiber to these institutions as part of the total modernization plan. Such plan shall include details of the rates to be charged education for use of the network. Institutions should be required to sign contracts, or otherwise demonstrate that they will utilize the fiber optic service and pay the rates determined, before construction is authorized. Such plan shall be submitted to the Commission within three months of this Order. The Commission further finds that all modernization investments must be completed within 54 months of the Order, and booked as completed.

V. INCENTIVE REGULATION PROPOSALS

In this proceeding, both USWC and the Division made proposals for the adoption of so-called "Incentive Regulation" plans in this jurisdiction. In essence, incentive regulation is based upon the assumption that traditional regulation does not provide sufficient incentives for regulated utilities to operate as efficiently as possible. Incentive regulation allows the utility to earn in excess of the authorized rate of return on equity with the hope that such overearnings will provide a greater incentive to management and employees to undertake additional efficiencies.

A. DISCUSSION OF PLANS

1. USWC PLAN:

The term of USWC's plan is four years, commencing January 1, 1991 and terminating December 31, 1994. During the term of the plan,

ADDENDUM B

STIPULATION AND JOINT MOTION
ON REVENUE REQUIREMENT ISSUES

OCTOBER 30, 1990

CONSOLIDATED DOCKET NOS. 90-049-03 & 06

APPROVED BY COMMISSIONERS *See*
BRIAN L. STEWART _____ *ord*
JAMES M. DYER _____ *af*
STEPHEN F. MECHAM _____ *1/3/91*

-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

In the Matter of the Application)
of U S WEST Communications for)
Approval of an Incentive Regula-)
tion Plan.)

STIPULATION AND JOINT
MOTION ON REVENUE
REQUIREMENT ISSUES

In the Matter of the Investiga-)
tion into the Reasonableness of)
the Rates and Charges of U S WEST)
Communications.)

Docket No. 90-049-03

Docket No. 90-049-06

BACKGROUND

On March 2, 1990, U S WEST Communications (USWC) initiated Docket No. 90-049-03 by filing an Application seeking approval of an incentive regulation plan. On March 29, 1990, the Division of Public Utilities (DPU) initiated Docket No. 90-049-06 by filing a Petition seeking an investigation into the reasonableness of the rates and charges of USWC and seeking an interim reduction in USWC's rates and charges. The cases were consolidated for purposes of hearing.

Hearings were held on May 24 and 25, 1990 on the request for an interim rate reduction. Testimony was filed by the DPU, the Committee of Consumer Services (CCS), and USWC. On June 22, 1990, the Commission issued its Order on interim rates, ordering that USWC reduce its intrastate rates by \$10.655 million. As implemented, the interim reduction totalled \$10.711 million.

Thereafter, the Commission established hearing dates in December 1990 to hear issues relating to revenue requirement and

incentive regulation. Rate spread hearings were scheduled to commence on February 28, 1991.

The DPU has engaged in extensive discovery on revenue requirement issues. The CCS also engaged in discovery on revenue requirement issues. In a prehearing conference held on August 1, 1990, the Commission encouraged the parties, in light of the Commission's October 18, 1989 revenue requirement decision in Docket No. 88-049-07, to resolve revenue requirement issues. Commencing with a scheduled settlement conference held on August 31, 1990, USWC, the DPU, and the CCS engaged in negotiations to resolve as many revenue requirement issues as possible and to reach agreements that will streamline the hearings and thus conserve the resources of the Commission and the parties. As a result of meetings subsequent to the August 31 settlement conference, USWC, the DPU and the CCS were able to reach agreement on all but a few revenue requirement issues. The Stipulation was then distributed to all parties of record.

STIPULATION

Based on the foregoing and in a good faith attempt to resolve as many revenue requirement issues as possible, the undersigned parties to this proceeding, USWC, the DPU, the CCS, hereby agree and stipulate as follows:¹

¹ Prior to filing this Stipulation and Joint Motion on Revenue Requirement Issues, the other parties to this proceeding, Tel America of Salt Lake City, Inc. (Tel America), McCaw Cellular

1. Statutory Support for Settlements. Section 54-7-1, Utah Code Annotated, encourages the settlement of disputed matters:

(1) Informal resolution, by agreement of the parties, of matters before the commission is encouraged.

(2) The commission may approve any agreement after considering the interests of the public and other affected persons.

(3)(a) At any time before or during a hearing or proceeding before the commission, the parties, between themselves or with the commission or a commissioner, may engage in settlement conferences and negotiations.

(b) The commission may adopt any settlement proposal of the parties and may enter an order based upon the proposal.

2. Unresolved Issues. The parties have resolved all issues relating to the calculation of revenue requirement in this matter, with the exception of the following:

- a. Rate of Return on Equity.
- b. Capital Structure.
- c. Depreciation Represcription.

3. Rate of Return on Equity and Capital Structure. The issues of Rate of Return on Equity and Capital Structure shall be presented to the Commission in the hearings scheduled to commence on December 10, 1990 ("the December hearings"). With regard to the Capital Structure issue, the expert witness for the CCS has

Communications, Inc. (McCaw), MCI Telecommunications, Inc. (MCI), the Exchange Carriers of Utah (ECU), Contel of the West (Contel), AT&T Communications of the Mountain States (AT&T), the Utah Cable Television Association (UCTA), Justin C. Stewart, George L. Gygi, A. Earl Cox, Barbara Toomer, Ronald Turpin, and Pat Coryell, were advised of this Stipulation. The parties who have joined in the Stipulation have so indicated by their signatures below.

indicated that he has questions, among them the differences between the Capital Structure proposed by USWC and the Capital Structure of U S WEST, Inc. The CCS has indicated a need to review additional information before making a specific recommendation on Capital Structure. USWC has provided the information requested to date by the CCS. Once that information and any other data requests have been reviewed by the CCS and its experts, the parties agree to work, in good faith, to attempt to either resolve disagreements regarding Capital Structure or clarify the extent of any disagreement. To the extent the parties are able to resolve or clarify Capital Structure issues, they shall immediately notify the Commission.

4. Depreciation Represcription. USWC's depreciation rates shall be established in this proceeding. However, the issue of Depreciation Represcription cannot yet be resolved because the depreciation studies will not be available until early November 1990. When these studies become available in early November, the parties agree to review them in an expeditious manner and, in good faith, attempt to reach an agreement on depreciation rates to be effective on January 1, 1991 and thereafter. In the event agreement on new depreciation rates is reached prior to the December hearings, the revenue impact of such changes will be presented by stipulation and presented to the Commission in the December hearings. In the event agreement cannot be reached on depreciation rate increases, the parties will litigate the matter as part of the rate design hearings scheduled to commence on

February 28, 1991 ("the spread hearings") so that the matter will be resolved prior to and incorporated in the Commission final order in this proceeding.

5. Joint Exhibit 1. The parties have jointly developed the exhibit attached hereto as Joint Exhibit 1 (JE-1), which sets forth the adjustments that the parties have agreed to and which the Commission should incorporate into its final revenue calculation in this case. For illustrative purposes, the parties have calculated JE-1 using six months actual results which have been annualized and normalized and the most recently found rate of return on equity, USWC's current actual capital structure, and with no increase in depreciation rates. The final calculation of revenue requirement will use updated results, as described below, the Rate of Return on Equity and Capital Structure found reasonable by the Commission following the December hearings, and any change in depreciation rates stipulated by the parties or found reasonable by the Commission following the spread hearings. The DPU conducted extensive discovery in the affiliated interest area. The CCS also engaged in some discovery on affiliated interest issues. Because certain studies could not be completed within the time frame of this proceeding, total analysis of all affiliate issues could not be completed. However, the parties believe the adjustments on affiliates set forth in JE-1 represent a reasonable resolution of this issue for purposes of this case. In the case of Post Retirement Benefits (PRB), the annual impact of the PRB obligation for current service (calculated to be \$2.568

million on a Utah intrastate basis for 1991) ("Current PRB") shall be included in the final revenue requirement calculation in this case. USWC agrees to book and fund the Current PRB expense effective January 1, 1991. Workpapers supporting the calculation by USWC's actuary of the intrastate expense for Current PRB shall be provided to the DPU and CCS for audit and review. Not later than thirty days from the date the workpapers are delivered to the DPU and CCS, the DPU and CCS shall notify USWC if they do not agree with the calculation and shall identify any reasons for their disagreement. In the event of a disagreement on the calculation, the parties shall attempt, in good faith, to resolve the disagreement. If they are unable to resolve the disagreement, the issue of the proper amount of Current PRB will be litigated in the December hearings. However, in no event will any disagreement regarding the calculation of Current PRB affect the parties' stipulation that the annual impact of Current PRB shall be included in the final revenue requirement calculation in this case. The parties' stipulation to a \$2.568 million adjustment to test-year expenses for Current PRB will be updated to reflect the requirements of any Statement on Current PRB issued by the Financial Accounting Standards Board (FASB) prior to the spread hearings. However, the parties agree that the revenue requirement adjustment and booking of PRB will not be deferred if the Statement permits employers to defer commencement of the booking of Current PRB to a date later than January 1, 1991. This Stipulation does not address the issue of prior service PRB costs.

6. Updates To JE-1. The parties agree that several of the columns in JE-1 shall be updated monthly with additional actual data. At the time of the December hearings, the parties will provide the latest updated JE-1 which will present nine months actual results on an annualized and normalized basis consistent with the annualization and normalization of six month's actual data in JE-1. The method of calculation shall be the same as in Exhibit JE-1. Subsequent monthly updates will be provided to the Commission.

7. Specific Items to be Updated. All columns on JE-1 shall be updated, with the exception of the following:²

Column 2: Prior Period SNFA

Column 3: Antitrust-General Dynamics

Column 4: 5 + 5 Curtailment Gain

Column 5: Prior Period Independent Company Settlements

Column 6: Amortization-Embedded \$200-\$500

Column 7: Annualization of 5 + 5 Savings

Column 8: Annualization of Rent Compensation

Column 9: Annualization of Universal Service Fund

Column 10: Annualization of Wage Increases

Column 11: Annualization of Management Concession Changes

Column B: Lobbying

Column C: PAC and Shareholder

Column I: Antitrust

² The parties understand that this Stipulation shall not affect any reporting requirements of USWC heretofore ordered by the Commission.

Column J: Advertising

Column M: 1991 Separations Shifts

Column N: Reserve Deficiency Amortization

Column O: Riser Cable Amortization

Column P: Increase in Travel and Oil Expenses

Column Q: Interim Rate Decrease

Column S: Service Link

Column T: Bellcore

Column U: Affiliate ROE and Depreciation

Column V: Other Affiliates

8. January 1, 1991 Interim Rate Reduction. In order to implement this Stipulation, USWC shall, effective January 1, 1991,³ reduce its rates by \$8.238 million on an interim basis, subject to surcharge pursuant to Section 54-7-12(3)(b)(ii), Utah Code Annotated, if the final order reduces rates by less than the \$8.238 million interim adjustment. The \$8.238 million reduction reflects the net of Separations Shifts (Column M), the end of the Reserve Deficiency Amortization (Column N), and the end of the Riser Cable Amortization (Column O). The interim reduction shall be spread consistent with paragraph 3 of the Stipulation of June 20, 1990 in the following manner:

The reduction shall be spread on an even-percentage basis to recurring rates among and within the following categories:

³The portion of the interim reduction with respect to Residential and Business Local Exchange Services shall be made effective January 1, 1991. The portion of the interim reduction with respect to Toll Services and Switched Access Service shall be made effective January 15, 1991.

(1) Residential and Business Local Exchange-Services (dial-tone line, local usage, hunting, and Extended Area Service).

(2) Toll Services (message toll service, 800 Service, Out WATS).

(3) Switched Access Service (excluding billing and collections) by reducing both the originating and terminating carrier common line (CCL) by the overall percentage reduction for the category.

This agreement does not preclude parties from stipulating to an alternative spread of rates, subject to the Commission's approval.

9. Implementation of Final Order. Further adjustment in the rates will be implemented following the spread of rates hearings when the Commission issues its final order in this proceeding. The final order will incorporate any change in revenue requirement resulting from (i) the Commission's decision on Rate of Return on Equity and Capital Structure, (ii) the parties' stipulation or the Commission's decision on Depreciation Represcription, (iii) updating JE-1 for at least 11 months actual test year results and (iv) any update to PRB as provided in paragraph 5 above.

10. Rate Spread Targets. The parties recognize that the final revenue adjustment may not be quantified until after the spread hearings. To facilitate meaningful testimony from the parties on spread issues, the parties recommend that the Commission adopt the following procedures for the rate spread

portion of this case:

a. The Division will file its DCOS study and USWC will file its long run incremental cost (LRIC) studies on December 10 as currently scheduled (or at such later time as necessary). The filing of direct testimony on specific rate spread proposals will be deferred until January 21, 1991.

b. As soon as possible after the December hearings, the Commission will provide the parties with the range within which it foresees that final rate adjustments will fall, so that the parties will be providing spread testimony using the same general targets, thus assuring that the proposals of the parties are comparable.

c. For purposes of the specific rate spread testimony, the parties will use the rates in effect as a result of the June 1990 interim reduction of \$10.711 million as the base rate levels.

11. Public Interest. For the most part, the adjustments on JE-1 are consistent with adjustments or with methodologies adopted in Docket No. 88-049-07. Many of them would not be the subject of dispute if all revenue requirement issues were to go to hearing. However, several of the adjustments set forth in JE-1 would be disputed if this matter were not settled. The settlement of revenue requirement issues in the manner set forth on JE-1 represents a balanced approach to the revenue requirement issues resolved and will result in rates that are just and reasonable and in the public interest. The acceptance by the Commission of

this Stipulation will simplify the hearings in December and will conserve the resources of all parties, while at the same time promoting the interests of ratepayers of USWC and the citizens of the State of Utah.

12. Integrated Stipulation. The purpose of this Stipulation is to settle in their entirety, all revenue requirement issues, with the exception of those set forth in paragraphs 2, 3, 4, and that part of paragraph 5 relating to the quantification of Current PRB expense, for purposes of this case. By entering this Stipulation, none of the parties waives or otherwise prejudices its ability to propose or contest financial or accounting adjustments or other positions which are inconsistent with this Stipulation in future dockets before the Commission. The Stipulation is an integrated agreement, the provisions of which are dependent upon each other. Therefore, if it is not accepted in its entirety, the parties are free to withdraw therefrom.

13. Review/Rehearing and Appeal. Nothing in this Stipulation shall bar or be deemed to bar any party from seeking review and rehearing or judicial review of any aspect of the Commission's final order in these consolidated proceedings except with respect to matters expressly agreed to in this Stipulation.

JOINT MOTION

Based on the foregoing, the undersigned parties move that the Commission enter an Order approving the foregoing Stipulation in its entirety.

Dated this 30th day of October, 1990.

U S WEST Communications

by Kirk R. Nelson
Kirk R. Nelson
Assistant Vice President and
Director-External Affairs

by Ted D. Smith
Ted D. Smith
Chief Counsel-Utah

Division of Public Utilities

by Frank Johnson
Frank Johnson
Director

by Laurie L. Noda
Laurie L. Noda
Assistant Attorney General

Committee of Consumer Services

by Joseph L. Ingles
Joseph L. Ingles
Administrative Secretary

by Kent Walgren
Kent Walgren
Assistant Attorney General

Tel America of Salt Lake City

by _____

McCaw Cellular Communications

by _____

MCI Telecommunications

by _____

The Exchange Carriers of Utah

by _____

Contel of the West

by _____

AT&T Communications

by _____

Utah Cable Television Association

by _____

Justin C. Stewart, George L. Gygi,
A. Earl Cox, Barbara Toomer,
Ronald Turpin, and Pat Coryell

by _____

U S WEST COMMUNICATIONS
1990 UTAH INTRASTATE OPERATIONS
ANNUALIZED 6 MONTHS ACTUALS
DOCKET 90-049-06
(000)

33070535

10/09/90

	(1) 1990 ACTUAL JUNE 1990 YTD	(2) PRIOR PERIOD SNA	(3) ANNUALIZED GENERAL DYNAMICS	(4) S+5 CURTAILMENT GAIN	(5) PRIOR PERIOD IND CO SETTLEMENTS	(6) AMORT \$200-\$500 EMBEDDED	(7) ANNUALIZED S+5 SAVINGS	(8) ANNUALIZED RENT COMP	(9) ANNUALIZED UNIVERSAL SERV FUND	(10) ANNUALIZED WAGE INC	(11) ANNUALIZED MORT CONCESSION	(12)	(13)	(14) ADJUSTED ACTUAL RESULTS	(15) ANNUALIZED ACTUAL RESULTS
1 LOCAL SERVICE	94,190	(821)								0	28			94,219	107,427
2 NETWORK ACCESS	7,961													7,142	14,379
3 LONG DISTANCE	40,681				(662)			(1,200)						40,023	80,103
4 MISCELLANEOUS	16,320													15,120	31,120
5 TOTAL OP REVENUE	159,153	(621)	0	0	(662)	0	0	(1,200)	0	0	28	0	0	155,458	312,935
6 MAINTENANCE	25,945			1,894						69				27,909	55,817
7 ENGINEERING	2,624									56				2,680	5,359
8 NETWORK OPERATIONS	2,463									1				2,464	4,928
9 NETWORK ADMIN	1,415									27				1,442	2,884
10 ACCESS CHARGE	4,180	(245)							(500)			0		3,960	7,320
11 OTHER SVC & PROD	55									176				231	461
12 CUSTOMER OP	19,005						(823)			138				18,320	36,639
13 CORP OPERATIONS	19,555													19,555	39,111
14 PROPERTY TAX	8,564													8,564	17,128
15 UNCOLLECTIBLES	1,003													1,003	2,003
16 OTHER OP INC & EXP	41		0	0	0	0	0	0	0		0			41	81
17 DEPRECIATION	39,990					43								40,033	80,066
18 TOTAL OP EXPENSE	125,465	(245)	0	1,894	0	43	(823)	0	(600)	467	0	0	0	126,201	252,422
19 NORMALIZED FLT	5,906	(186)			(214)	(14)	266	(388)	194	(151)	9			4,910	9,821
20 NORMALIZED SIT	1,375	(29)			(33)	(2)	41	(60)	30	(23)	1			1,206	2,411
21 TOTAL OP TAXES	7,281	(215)	0	(707)	(247)	(16)	307	(448)	224	(174)	10	0	0	6,215	12,432
22 NET OP INCOME	26,407	(361)	0	(1,188)	(415)	(27)	516	(752)	376	(293)	18	0	0	24,281	48,562
23 NON-OP INCOME/EXP	13		(296)											(22)	(35)
24 NON-OP TAX	(70)													(72)	(12)
25 BATEMAKING INCOME	26,464	(361)	296	(1,188)	(415)	(27)	516	(752)	376	(293)	18	0	0	24,534	49,245
26 AFUDC														0	0
27 TOTAL INTEREST	8,590													8,590	17,180
28 NET INCOME FILED	17,875	(361)	296	(1,188)	(415)	(27)	516	(752)	376	(293)	18	0	0	16,045	32,025
29 AVERAGE RATE BASE															
30 PLANT IN SERVICE	997,747													997,747	997,747
31 MAT. & SUPPLIES	1,699													1,699	3,398
32 CASH WORKING CAP.	(14,103)													(14,103)	(14,103)
33 CORP. RESERVE	(386,362)													(386,362)	(386,362)
34 DEF TAXES (175)	(139,126)													(139,126)	(139,126)
35 CUSTOMER DEPOSITS	(2,088)													(2,088)	(2,088)
36 CONST CHRGD CONT.	(661)													(661)	(661)
37 TOTAL RATE BASE	453,106	0	0	0	0	0	0	0	0	0	0	0	0	453,106	453,106

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U.S. WEST COMMUNICATIONS
1990 UTAH INTRASTATE OPERATIONS
ANNUALIZED 6 MONTHS ACTUALS
DOCKET 90-049-06

JOINT EXHIBIT
31

PAGE 2

10/23/90	(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)	(J)	(K)	(L)	(M)	(N)	(O)
1990 TID	ANNUALIZED	LOBBYING	PAC & SHAREHOLDER CONTRIBUTIONS	CHARITABLE MEMBERSHIPS & DUES	INTEREST SYNCH	DIRECTORY IMPUTATION	UNCOLLECT	ANTITRUST	EXTERNAL RELATIONS ADVERTISING	AFUDC	CUSTOMER DEP	INTEREST ON SEPARATIONS RESERVE DEF RISKER CABLE AMORT	1991 SHIFT		
1 BUDGET/ACTUAL															
2 LOCAL SERVICE	188,437														
3 NETWORK ACCESS	14,279														
4 LONG DISTANCE	80,039														
5 MISCELLANEOUS	30,241					16,771									
6															
7 TOTAL OP REVENUE	312,995	0	0	0	0	16,771	0	0	0	0	0	0	0	0	0
8															
9 MAINTENANCE	55,917												545		
10 ENGINEERING	5,359												212		
11 NETWORK OPERATIONS	4,928														
12 NETWORK ADMIN	2,884														
13 ACCESS CHARGE	7,920														
14 OTHER SVCS & PROD	461														
15 CUSTOMER CP	36,639								(761)				335		
16 CORP OPERATIONS	39,111														
17 PROPERTY TAX	17,128														
18 UNCOLLECTIBLES	2,007														
19 OTHER OP INC & EXP	81						873						136		
20 DEPRECIATION	80,066												747	(10,000)	(1,110)
21															
22 TOTAL OP EXPENSE	252,402	0	0	0	0	0	873	0	(761)	0	0	0	1,976	(10,000)	(1,110)
23															
24 NORMALIZED FTT	9,821					(326)	(282)	(37)	246	0	0	0	(638)	3,230	350
25 NORMALIZED SFT	2,411					(50)	(44)	(4)	38	0	0	0	(99)	500	50
26															
27 TOTAL OP TAXES	12,032	0	0	0	0	(376)	(326)	(41)	284	0	0	0	(737)	3,732	400
28															
29 NET OP INCOME	48,561					0	(547)	41	477	0	0	0	(1,239)	6,270	700
30 NON-OP INCOME/EXP	(566)	(126)	(1)	(509)	(23)	0			0	968	179	(5)			
31 NON-OP TAX	(141)	47		227	9										
32															
33 RATEMAKING INCOME	49,268	79	1	382	14	376	(547)	41	477	(968)	(179)		(1,234)	6,270	700
34										968					
35 AFUDC						1,008		74			(179)				
36 TOTAL INTEREST*	17,179														
37															
38 NET INCOME FILED	32,089	79	1	382	14	(632)	(547)	(33)	477	0	0	0	(1,234)	6,270	700
39															
40 AVERAGE RATE BASE															
41 PLANT IN SERVICE	993,747												10,174		
42 MAT. & SUPPLIES	1,699												18		
43 CASH WORKING CAP.	(14,103)														
44 DEPR. RESERVE	(386,362)												(3,414)		
45 DEF TAXES (176)	(139,125)												(1,339)		
46 CUSTOMER DEPOSITS	(2,088)														
47 CONST. CREDIT CONT.	(661)														
48															
49 TOTAL RATE BASE	453,106	0	0	0	0	0	0	41	0	0	0	0	5,239	0	0
50															
51 RET. ON RATE BASE	10,874														
52 FINANCIAL RES.	11,804														
53 CASH STRUCTURE FOL	12,104														

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U.S. WEST COMMUNICATIONS
1990 UTAH INTRASTATE OPERATIONS
ANNUALIZED 6 MONTHS ACTUALS
DOCKET 90-049-06

9-PTC535

(000)

	(P) INCREASE TRAVEL & OIL EXPENSES	(Q) INTERIM RATE RED	(R) PAYMENT CENTER CLOSURE	(S) SERVICE LINK	(T) BELLCORE	(U) AFFILIATE ROE & DEPRECIATION	(V) OTHER AFFILIATES	(W) CURRENT PRB	(X)	(Y)	(Z)	(AA) ADJUSTED RESULT	(BB) (DECREASE) 11.80% ROE	(CC) FINAL RESULT
1 1990														
2 BUDGET/ACTUAL		(10,711)										177,726	(14,146)	163,579
3 LOCAL SERVICE												14,279		14,279
4 NETWORK ACCESS												80,039		80,039
5 LONG DISTANCE												47,012		47,012
6 MISCELLANEOUS														
7 TOTAL OP REVENUE	0	(10,711)	0	0	0	0	0	0	0	0	0	319,055	(14,146)	304,909
8 MAINTENANCE	35											56,398		56,398
9 ENGINEERING												5,571		5,571
10 NETWORK OPERATIONS												4,928		4,928
11 NETWORK ADMIN												2,884		2,884
12 ACCESS CHARGE												7,920		7,920
13 OTHER SVC & PROD												461		461
14 CUSTOMER CP												35,422		35,422
15 CORP OPERATIONS	25		(456)	(372)	(36)	(62)	(534)	2,568				41,035		41,035
16 PROPERTY TAX												17,128		17,128
17 UNCOLLECTIBLES												2,890	(47)	2,843
18 OTHER OP INC & EXP									0			217	(129)	88
19 DEPRECIATION	0											69,695		69,695
20 TOTAL OP EXPENSE	60	0	(456)	(372)	(36)	(62)	(534)	2,568				244,540	(175)	244,364
21 NORMALIZED FTL	(19)	(3,450)	147	120	12	20	172	(829)	0			13,755	(4,512)	9,242
22 NORMALIZED ST	(3)	(536)	23	19	2	3	27	(128)	0			3,053	(639)	2,413
23 TOTAL OP TAXES	(22)	(3,995)	170	139	13	23	199	(958)	0			16,858	(5,211)	11,647
24 NET OP INCOME	(38)	(6,716)	286	233	23	39	335	(1,610)	0			57,707	(8,759)	48,948
25 NON-OP INCOME/EXP						0						(183)		(183)
26 NON-OP TAX														
27 RATEMAKING INCOME	(38)	(6,716)	286	233	23	39	335	(1,610)	0			57,890	(8,759)	49,131
28 AFUDC												968		968
29 TOTAL INTEREST												18,082		18,082
30 NET INCOME FILED	(38)	(6,716)	286	233	23	39	335	(1,610)	0			40,776	(8,759)	31,017
31 AVERAGE RATE BASE												1,005,054		1,005,054
32 PLANT IN SERVICE					1,133		0					1,717		1,717
33 MAT. & SUPPLIES												(14,103)		(14,103)
34 CASH WORKING CAP.												(389,776)		(389,776)
35 DEPR. RESERVE												(140,624)		(140,624)
36 DEF TAXES (176)												(2,088)		(2,088)
37 CUSTOMER DEPOSITS												(661)		(661)
38 CONST. CHRGD CONT.														
39 TOTAL RATE BASE	0	0	0	0	1,133	0	0	0	0	0	0	459,519	0	459,519
40 RETURN RATE BASE												12,604		12,604
41 FINANCIAL ROE												15,004		15,004
42 CAP STRUCTURE POE												14,954		14,954

ADDENDUM C

ORDER ON REVIEW

AUGUST 13, 1991

CONSOLIDATED DOCKET NOS. 90-049-03 & 06

DOCKETED

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Application)	
of US WEST Communications for)	<u>DOCKET NO. 90-049-03</u>
Approval of an Incentive)	
Regulation Plan.)	
)	
In the Matter of the Investigation)	<u>DOCKET NO. 90-049-06</u>
into the Reasonableness of the)	
Rates and Charges of US WEST)	<u>ORDER ON REVIEW</u>
Communications)	

ISSUED: August 13, 1991

BY THE COMMISSION:

By its Petition filed July 19, 1991, US WEST Communications (the "Company") requested that the Commission review and reconsider its Report and Order of June 19, 1991 in these two Dockets. In particular the Company argued that the Commission should reconsider certain aspects of its Order as follows:

1. The Commission should reconsider its interpretation of the parties' Stipulation on revenue requirement issues in that it is contrary to the intent of the parties.

2. The Commission should reconsider its order on network modernization in that it exceeds the Commission's authority, is not supported by the record, is a result that no party sought and deprives the Company of due process.

3. The Commission should reconsider the proposed incentive plan.

4. The Commission should reconsider the standards it adopted for interim decreases.

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5. The Commission should grant a stay of \$5.916 million of the rate decrease ordered.

6. The interim spread of the rate reductions to WATS and 800 services should become permanent.

The Committee of Consumer Services (the "Committee") also filed a request for review and reconsideration of certain aspects of the Commission's Order:

1. The Commission should reconsider the rate of return awarded if the Company opts out of the proposed incentive plan.

2. The Commission should reconsider its offer of an incentive plan because it has not made a finding that the rates under such a plan would be just and reasonable.

3. The Commission should reconsider its refusal to require the Company to provide data regarding the costs of developing, advocating and litigating the Company's proposed incentive plan.

4. The Commission should reconsider its adoption of an incentive plan in view of the constitutional challenge to the incentive plan statute.

5. All of the discussion in the Report and Order should be considered findings.

Finally, Intervenor-Petitioners filed a petition for reconsideration of certain aspects of the Commission's Order:

1. The Commission should reconsider the constitutionality of § 54-4-4.1.

2. The Commission should reconsider the increase in the Company's rate of return.

3. The Commission should reconsider its adoption of an incentive plan.

4. The Commission should reconsider the effective date of the incentive plan.

The Commission held a hearing to take oral argument on the petitions for reconsideration and based upon the filings and the argument presented makes the following ruling.

First with regard to the issues raised by the Company.

1. The Commission should reconsider its interpretation of the parties' Stipulation on revenue requirement issues in that it is contrary to the intent of the parties. The Company takes the position that the Stipulation as implemented in the Commission's Order does not represent the Company's understanding of its intent and meaning. According to the Company, standard rate-case annualizing and normalizing adjustments to actual 1990 performance data were contemplated by the Stipulation. At hearing, and again in review, it became obvious that the Division, the Company, and the Committee had different interpretations of the provisions of the Stipulation. The Committee's view of the Stipulation is the one the Commission finds most reasonable and which most closely resembles the plain meaning of the Stipulation as a whole. By forbidding updated information to be inserted into certain of the defined categories of Exhibit JE-1, submitted as an addendum to the Stipulation, and by limiting it to the others, paragraphs six and

seven, the Stipulation provides definition, certainty and finality, which permits the parties to devote limited resources to more pressing issues. To allow for the addition of new categories, as the Company suggests, makes the Stipulation vulnerable to endless debate and discovery, the very problems that stipulations are intended to avoid.

The Company calls unfair the correction made by the Commission to the annualization of the interim rate decrease category of Exhibit JE-1, asserting that the Commission has done what it has prohibited the Company from doing. However, as we tried to make clear in the Order, the interim rate decrease as shown on Exhibit JE-1 was incorrectly stated and we merely rectified it--we did not update it.

2. The Commission should reconsider its order on network modernization because it exceeds the Commission's authority, is not supported by the record, is a result that no party sought and deprives the Company of due process. As noted in our June 19, 1991 Order, the Company has been successful in selling us on the benefits and need for modernization of the network. Now that the Commission has determined that modernization is in the public interest and ordered that it be accomplished, but without the incentive plan the Company said it wanted, the Company argues that the Commission was obligated to tell it that the adequacy of network facilities would be an issue so that it could respond, otherwise the Company says it is deprived of due process. It strikes us--that this is an amazing twist of the record.

proposing the modernization, the Company put the adequacy of the system, central offices, backbone transmission, and rural distribution facilities, squarely in issue. The Company could not expect realistically that the Commission would approve an investment the size of the Company's proposed modernization and saddle ratepayers with the costs, if the present system were adequate. The Company has well demonstrated through its own witnesses and the public witnesses it orchestrated, that the network is not adequate to meet present and future public requirements and needs to be upgraded. We believe the Company has itself met the burden of showing inadequacy of the system, whether it intended to do so or not. In addition, based upon testimony of Division, Committee, and public witnesses, we find that the record contains specific instances where the current system is inadequate.

Furthermore, there is virtually no risk to the Company. The Company has convinced us that modernization is a prudent and necessary course and it will be allowed to earn a just and reasonable rate of return on the investment. Normally, if a regulated utility undertakes an investment in infrastructure, it is subject to the risk of a prudence review before the investment is allowed in rate base. However, where the investment is mandated by the regulator, the risk is narrowed to the question of whether the investment has been implemented in a prudent manner. We have no reason to think that the Company would not be prudent in implementing this investment. All of its prior investments have been allowed by this Commission.

As we said in our Order, the Commission decides what is and is not an adequate network. Section 54-4-7 is clear on its face. We have held a hearing at which the need for modernization was an issue. On the basis of the record we have found and concluded that the present network is inadequate and an upgrade of facilities is needed; the benefits of modernization exceed the costs. The Company was not constrained to make the case for modernization; their presentation was wholly voluntary. The Company could have cross-examined public witnesses or further clarified the testimony of Company witnesses. For its own reasons it elected not to do so. If it is true, as the Company suggests, that because the Company has not proposed a modernization program without an incentive plan, we are now forced to ignore the considerable testimony in support of modernization, it would seem that the tail wags the dog.

We would note that if the modernization program is not accomplished, present rates will be excessive because we have allowed depreciation rates to reflect the remaining lives of old equipment commensurate with the upgrades and replacements in the modernization program.

We also note that both the Division and the Committee recommended in this case that rural central office upgrades be ordered without an incentive plan, so the Company cannot be heard to say that that upgrade was not in issue, even by its standard. Indeed, McCaw proposed that all upgrades be made, even without an incentive plan. The Division and the Committee each took the

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position that the distance learning investments should not be made until there was sufficient demand and economic justification and that was embodied in our Order; the Company has simply been ordered to create and supply us with a plan setting forth details, including rates, and demonstrating utilization for distance learning upgrades.

3. The Commission should reconsider the proposed incentive plan. The Company has requested that we reconsider the incentive plan set forth in our Order and adopt the features of the plan which the Company proposed. The Company views our proposed plan as riskier for it than traditional rate regulation and lacking any meaningful incentives. In our minds, however, the plan formulated by the Company would have shifted excessive risk to the ratepayer. We have attempted with our plan to balance the risk and still provide incentives. The Company is on record in this case as viewing incentive regulation as a means to a higher rate of return. Under the terms of the Commission's plan, the Company would be able to earn 14 percent, a rate it said would be reasonable during the rate case.

The Company has argued that under the terms of our proposed plan it would not be allowed to file a rate case during the course of the plan. We had not intended that result and so state. We will strike the last sentence on page 100 of our June 19, 1991 Order. The Company would be free to file a rate case at any point that it felt rates were inadequate.

We are satisfied that the plan we proposed is in the public interest and have not been convinced otherwise. The Company argues there is no support in the record for the plan we advanced; we disagree. Even if there were not, so far as the Company is concerned, we are not bound by what witnesses may propose in the way of an incentive plan. We are not obligated to provide or approve any incentive plan. If, in our discretion, we conclude that a particular plan will advance the public interest, we may approve or proffer a plan. The Company has an absolute protection by way of the veto provided to it by the Legislature.

4. The Commission should reconsider standards for interim rate decreases. The Company argues that the standards for interim decreases differ unfairly from those associated with interim increases. We have already discussed and ruled on the issue of interim decrease standards in our June 22, 1990 Order and see no reason to depart from our conclusions there. The ratepayers and the Company are situated differently in significant ways (something even Company Witness Kyritz admitted in this case) and, therefore, different standards are warranted.

5. The Commission should order a stay of \$5.916 Million of the rate decrease ordered. The Company previously requested a stay of the entire amount of the rate reduction and we determined not to grant a stay for reasons set forth at that time. While the Company has delineated more precisely the amount it is contesting, the Commission is still not inclined to grant a stay since we are persuaded that a surcharge can be ordered. The Company may or may

not elect to appeal from our decision. If they do not, any stay granted by this Commission would be moot. If they do, the Supreme Court will doubtless be asked to rule on the issue.

6. The interim spread of the rate reductions to WATS and 800 Services should become permanent. The Commission will adopt the interim rate structure proposed by the Company as the permanent rate structure for WATS and 800 services, it appearing reasonable and no party objecting. However, the Company is directed hereby to provide the Commission within 90 days with the cost data for modifying the billing procedures for these services as proposed by the Division.

The Commission rules on the Committee's petition for reconsideration as follows:

1. The Commission should reconsider the rate of return awarded if the Company opts out of the proposed incentive plan. The Committee argues that if the Company opts out of the incentive plan proposed by the Commission, the Commission should lower the rate of return from 12.2 percent to 11.8 percent. The Commission's discussion and findings set forth in its June 19, 1991 Order adequately address the reasons for setting the rate of return at 12.2 percent. These reasons have nothing to do with the adoption of an incentive plan.

2. The Commission should reconsider its offer of an incentive plan because it has not made a finding that the rates under such a plan would be just and reasonable. The Committee takes the position that the record does not support a finding that

the Commission's proposed incentive plan will produce just and reasonable rates. We disagree. The incentive plan will be experimental, but common sense suggests that its characteristics will eliminate most if not all of the risks of incentive regulation to ratepayers and will in all likelihood result in benefits which could not be achieved under traditional regulation (e.g. the retroactive capture of overearnings). We consider that the June 19, 1991 Order adequately addresses the issue of an incentive plan and supplies adequate findings.

3. The Commission should reconsider its refusal to require the Company to provide data regarding the costs of developing, advocating and litigating the Company's proposed incentive plan. The Committee has not raised any argument different from those it previously raised in support of its petition and, therefore, the Commission is not persuaded that it should rule differently than it did before.

4. The Commission should reconsider its adoption of an incentive plan in view of the constitutional challenge to the incentive plan statute. As we stated in response to Intervenor-Petitioners' request for a declaratory order, the Commission must presume the constitutionality of legislative enactments. It is for the Courts to determine the constitutionality of the incentive legislation. We have fashioned an incentive plan based on our assumption that the legislation is valid constitutionally. If the Court ultimately rules to the contrary, we will govern ourselves accordingly.

5. All of the discussion in the Report and Order should be considered findings. The Commission is not a court of law. We do not evaluate issues in the way a court would. We do not take and consider evidence in the same way. It is true that we have quasi-judicial functions at times but as an administrative arm of the Legislature, we also have quasi-legislative and ongoing administrative responsibilities. We do not have the luxury of deciding a case and having done with it. That means that public policy concerns, informed judgment and forecasting always play a part in our determinations. We intend by this to draw attention to the fact that our orders are not going to be precisely like a Court's orders. The discussion portion of our orders is important as it relates to the conclusions we reach, i.e., contains support for our findings and conclusions. So-called "findings" are bolded for convenience of parties, not because they constitute the only relevant parts of an order. If the Legislature intends that we operate as a court and that our orders be constructed like a court's in all respects, then it must alter the way utilities are regulated.

We address the Intervenor-Petitioners' reconsideration requests as follows:

1. The Commission should reconsider the constitutionality of § 54-4-4.1. Intervenor-Petitioners reargue the constitutionality of the incentive regulation statute. We have clearly stated by earlier order our position that the Commission has no authority to consider and pass on the constitutionality of

legislative enactments. We have been presented no argument on review that persuades us that we should change our position.

2. The Commission should reconsider the increase in the Company's rate of return. Intervenor-Petitioners argue, as have the Committee, that the rate of return should be lowered to 11.8 percent. We have already dealt with this issue in connection with the Committee's petition for review and refer to that discussion.

3. The Commission should reconsider its adoption of an incentive plan. Intervenor-Petitioners argue that there are substantial administrative law and constitutional problems with the plan adopted by the Commission under § 54-4-4.1 in addition to the facial unconstitutionality of that statute. We rely on our discussion hereinabove and in the June 19, 1991 Order as justification for the proposed incentive plan.

4. The Commission should reconsider the effective date of the incentive plan. Intervenor-Petitioners assert that there is serious ambiguity with establishing the date upon which the Commission's Order becomes final for purposes of reconsideration and judicial review. We have already dealt with this issue in considering Intervenor-Petitioners' petition for clarification and refer to that discussion. Intervenor-Petitioners also suggest that it is not clear whether the Company can reject only the incentive plan proffered by the Commission or the entire order. We do not share the view that the statute is ambiguous in that regard. It seems very clear on its face that the statute allows the Company to

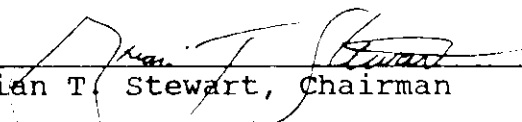
- 13 -

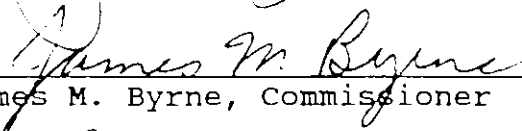
reject only those provisions of a Commission order which would require the Company to share revenues with ratepayers.

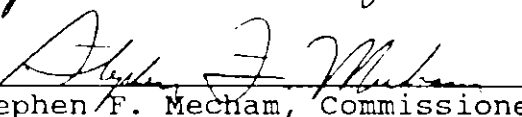
ORDER

NOW, THEREFORE, the Commission having considered the issues raised for reconsideration by parties in this proceeding, reaffirms its Order save for the clarification of the WATS and 800 service spread, the requirement of cost data in connection with WATS and 800 service and the clarification of the incentive plan proposed by the Commission as set forth hereinabove. The parties now have 30 days within which to petition the Supreme Court for review of the Commission's June 19, 1991 Order. However, the incentive plan portion of the Order will not become final for purposes of review until August 19, 1991, or until the Company accepts the incentive plan, whichever first occurs.

DATED in Salt Lake City, Utah this 13th day of August, 1991.


Brian T. Stewart, Chairman


James M. Byrne, Commissioner


Stephen F. Meacham, Commissioner

ATTEST:


Stephen C. Hewlett
Commission Secretary

005707

ADDENDUM D

SURREBUTTAL TESTIMONY AND
EXHIBITS OF PHILIP SELANDER

CONSOLIDATED DOCKET NOS. 90-049-03 & 06

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application)	Docket No. 90-049-03
of U S WEST Communications for)	Written Surrebuttal
Approval of an Incentive)	Testimony of
Regulation Plan)	PHILLIP S. SELANDER

In the Matter of the Investigation)	Docket No. 90-049-06
into the Reasonableness of the)	
Rates and Charges of U S WEST)	
Communications)	

February 15, 1991

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PROPRIETARY VERSION

THIS VERSION OF MR. SELANDER'S TESTIMONY CONTAINS PROPRIETARY EXHIBITS AND SHOULD BE RELEASED ONLY TO PERSONS WHO HAVE ENTERED THE PROTECTIVE ORDER. PLEASE CONTACT TED SMITH (801-237-7415) FOR A LIST OF PERSONS WHO HAVE ENTERED THE PROTECTIVE ORDER.

1 Q. PLEASE STATE YOUR NAME.

2 A. My name is Phillip S. Selander.

3 Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

4 A. The purpose of this testimony is to respond to portions of the rebuttal
5 testimony on incentive regulation and the direct testimony in rate
6 design of William Dunkel. I also address some of the issues raised by
7 the Commission in the November 4, 1990 Scheduling Order.

8 RESPONSE TO MR. DUNKEL'S REBUTTAL TESTIMONY ON INCENTIVE REGULATION

9 Q. HAS MR. DUNKEL INTRODUCED ANY NEW CONCEPTS IN HIS REBUTTAL TESTIMONY?

10 A. Not really. For the most part, he has repeated the same erroneous
11 concepts that were in his direct testimony.

12 Q. WHAT ARE THE MAJOR ERRORS IN MR. DUNKEL'S REBUTTAL TESTIMONY THAT YOU
13 WILL ADDRESS IN THIS TESTIMONY?

14 A. The following are the major errors that I will address in this
15 testimony:

- 16 • Mr. Dunkel's claim that costs will continue to decline in the
17 telecommunications industry.
- 18 • Mr. Dunkel's claim that the office modernizations are mandatory
19 because of the plan to introduce interchangeable codes in 1995.

- 1 • His claim that the office modernization should be completed
2 without incentive regulation because such changes are happening
3 throughout the industry.
- 4 • His conclusion that the office modernizations are economical and
5 that the Commission should order USWC to do the modernization with
6 or without incentive regulation.

7 Q. MR. DUNKEL STATES THAT, "THE COST OF PROVIDING TELEPHONE SERVICE IS
8 DECLINING IN UTAH" AND THAT "THE COST OF PROVIDING TELEPHONE SERVICE
9 WILL CONTINUE TO DECLINE IN UTAH." (DUNKEL REBUTTAL, PAGE 10) DO YOU
10 AGREE WITH HIS STATEMENTS?

11 A. No. His basic premise that the costs to provide telephone service will
12 continue to decline is based on only one factual premise, that equipment
13 costs are declining. From this one point, he makes a broad
14 extrapolation about overall costs that he fails to support with
15 evidence. Even though it is true generally that the telecommunications
16 industry has experienced reductions in equipment costs due to both
17 technology and to increased competition among manufacturers, this does
18 not mean that trends of lower equipment costs will continue
19 indefinitely. Also, just because some equipment costs are declining
20 does not mean that overall costs of providing telephone service are
21 declining, or that the overall costs will decline. I addressed this in
22 detail in my rebuttal testimony. Ms. Kyritz has addressed this issue in
23 her December testimony and in her surrebuttal testimony on incentive
24 issues.

1 Q. MR. DUNKEL USES SOME EXAMPLES OF LOWERING EQUIPMENT COSTS. PLEASE
2 RESPOND TO HIS STATEMENTS.

3 A. Mr. Dunkel makes two specific points regarding equipment costs that need
4 to be clarified to correct some overgeneralization:

5 Statement: "'Subscriber carrier' reduces the number of cable
6 pairs which are needed. Subscriber carrier concentrates the
7 traffic from a large number of customers onto only a few cable
8 pairs. Instead of adding a new cable to serve additional
9 customers, the Company now can just add electronic equipment.
10 This reduces the need for new cable, reduces the number of cable
11 pairs which must be maintained and is more efficient." (Dunkel
12 Rebuttal, page 18)

13 Response: The deployment of subscriber carrier in the local loop has
14 enabled USWC to realize some significant capital savings in comparison
15 to copper cable alternatives. However, subscriber carrier usually
16 becomes an economical alternative to reinforce areas that are long
17 distances from the central office. For distribution facilities, and
18 for feeder facilities required closer to the central office, copper
19 cable is still in many situations the most economical alternative.

20 In claiming that "the Company now can just add" electronic equipment,
21 Mr. Dunkel implies that there is no significant cost to do so. In fact,
22 it costs over \$50,000 per 96 channel system (including the central
23 office terminal, remote terminal, and electronic cards). The copper
24 cable must be conditioned in order to support subscriber carrier. This
25 conditioning requires the placing of repeater cards approximately every
26 3,000 feet depending upon the gauge of cable being utilized. The cost
27 per repeater location for an apparatus case and repeater cards is over

1 \$2,000. Also, not all existing copper cables can be utilized for
2 subscriber carrier. Copper cables must be in good condition, and the
3 cable must be large enough to ensure proper separation of the transmit
4 and receive pairs in order to avoid cross talk.

5
6 Statement: "One advantage of fiber optic facilities is that
7 additional traffic can be handled at a very small additional cost.
8 Once the fiber is installed, much more traffic can be handled
9 without installing more fiber. With fiber, additional traffic can
10 be handled at a small additional cost. . . This additional traffic
11 produce additional revenues but little additional cost. A large
12 portion of these additional revenues are profit." (Dunkel
13 Rebuttal, page 14)

14 Response: In most cases, the largest portion of the costs associated
15 with fiber facilities is the electronic equipment costs. Relative to
16 copper cable, fiber cable is inexpensive. For example, the loaded per
17 foot cost of a 4 fiber cable is under \$2.00. The capacity of the 4
18 fiber cable, depending on the multiplexing system used, would be from
19 672 circuits (45 megabit system) to 16,128 circuits (1.12 gigabit
20 system). In comparison, a 1200 pair (1200 circuits) 22 gauge copper
21 cable has a loaded cost of over \$13.00 per foot.

22 The electronics, on the other hand, are expensive. For example, the
23 loaded cost of the electronics for a 45 megabit system is approximately
24 \$60,000, and approximately \$550,000 for a 1.12 gigabit system. After a
25 system is first installed, growth circuits can usually be accommodated
26 by adding additional electronic cards. The cost of adding individual
27 cards is relatively inexpensive in relation to the total cost of the
28 system. However, usually more than 50% of the total cost of a fully

1 equipped fiber system is attributed to the electronic card costs. When
2 the existing system reaches capacity, an additional system is required.
3 Therefore, whether increased traffic triggers major costs, depends upon
4 the existing spare capacity of the electronic equipment. Whether
5 additional profits are achieved depends upon the costs required to
6 support additional traffic.

7 Q. IN HIS REBUTTAL TESTIMONY, MR. DUNKEL MAKES SEVERAL POINTS REGARDING THE
8 COSTS AND BENEFITS OF VARIOUS CENTRAL OFFICE TECHNOLOGIES. PLEASE
9 RESPOND TO THE POINTS THAT HE MAKES.

10 A. I will list each statement and then respond to them:

11 Statement: "Routine maintenance costs of digital switches are
12 greatly reduced." (Dunkel Rebuttal, page 17)

13 Response: This statement is true. However, maintenance costs are only
14 one of the many elements considered in an economic study. Higher
15 maintenance costs in existing technology do not make a modernization
16 alternative an economic winner. Many other factors must be taken into
17 account. Also, USWC has been able to significantly reduce the
18 maintenance cost of electromechanical offices by installing Call-Pro
19 equipment, and by using electronic step-by-step equipment for growth
20 additions. Call-Pro equipment electronically decodes the customer dial
21 digits and greatly reduces the movement of the first selector, which in
22 turn reduces the wear on the first selector.

1 Statement: "With digital central office equipment, it is
2 generally not necessary for a maintenance person to physically
3 travel to the digital central office for a service order.
4 Instead, the changes required are remotely input to that central
5 office from a location which may be miles away. With the
6 electromechanical switching equipment, it is necessary for a
7 maintenance person to physically change wiring in the central
8 office." (Dunkel Rebuttal, page 17)

9 Response: Service order work can only be done remotely for an
10 electronic office if the DIP (dedicated inside plant) concept has been
11 used. Otherwise, a frame person must be dispatched to accomplish the
12 frame connection. In order to implement DIP in an office, more
13 equipment must be used in order to prewire sufficient terminations.
14 Therefore, the DIP concept will only be deployed in high activity
15 offices where significant cost savings can be realized. Currently, the
16 Provo central office is the only office where DIP has been deployed on a
17 large scale. To a much smaller degree, DIP is being deployed in other
18 offices. Therefore, most electronic offices will continue to require
19 on-premise personnel to complete service order work. Finally, even when
20 an office has 100% DIP, it does not eliminate entirely the need to visit
21 the community where the central office is located. Connections are
22 often required in the outside network. The time spent by telephone
23 installers who stop by the office to complete frame connections is
24 incidental to the overall time required to travel to and from the
25 community to complete the outside work.

26 Even though the Company has plans to significantly increase the
27 deployment of DIP in high activity offices such as Provo (which is
28 driven primarily by residence services relating to BYU students), DIP

1 will not be deployed in most of the electromechanical offices when they
2 are upgraded. The reason DIP will not be deployed in these offices is
3 because of their smaller size and relatively low activity.

4 The project to DIP an office is another example of a discretionary
5 project that must compete for funding with other discretionary projects.
6 In a business-as-usual environment, the project to provide DIP in an
7 electronic office could end up ranking higher than the project to
8 upgrade an electromechanical office.

9
10 Statement: "A digital central office is more trouble free than an
11 electromechanical office. In the cases that I am aware of the
12 trouble rates have been cut in half when an electromechanical
13 office was replaced by a digital office. This means less Company
14 personnel are needed to receive customer complaints, make repairs,
15 etc." (Dunkel Rebuttal, page 18)

16 Response: It is true that a digital office is more trouble free than an
17 electromechanical office. But the personnel costs to receive complaints
18 and to make repairs are factored into economic studies. These costs are
19 only a few of the many elements contained in an economic study. In most
20 situations, higher repair costs in the existing technology does not make
21 the modernization alternative an economic winner.

22 Q. THE TESTIMONY OF THE COMMITTEE AND TO A LESSER EXTENT THE TESTIMONY OF
23 THE DIVISION IMPLIES THAT THERE ARE MAJOR SERVICE PROBLEMS WITH THE
24 ELECTROMECHANICAL OFFICES. PLEASE RESPOND.

25 A. The Committee and the Division have produced no factual evidence to
26 support that there are major service problems with the electromechanical

1 offices. The only information provided that could be misunderstood to
2 indicate that there are major problems with electromechanical offices is
3 information about trouble reports.

4 As shown on page 16 of my direct testimony, the report rate in Utah for
5 the twelve months ending August 1982 was 3.41 monthly reports per one
6 hundred lines (in other words, 3.41 monthly cases of trouble per one
7 hundred lines). The August 1982 report rate was the first twelve month
8 period during which reports were prepared on a basis comparable with
9 today. In 1990, the USWC Utah report rate was 1.49 monthly reports per
10 one hundred lines. In 1990, Idaho had the lowest report rate in USWC at
11 1.43. The highest report rate in the 14 state area was 2.61. Utah had
12 the third lowest report rate. Also, Utah's report rate was better than
13 the Washington report rate of 1.7. Washington has all electronic
14 offices. From the above figures it is clear that Utah has lowered its
15 report rate substantially since 1982 and now ranks close to the best in
16 the Company.

17 For 1990, the report rate for the 46 electromechanical offices was 2.86.
18 Furthermore, the 2.86 report rate for electromechanical offices is
19 significantly better than the Utah report rate in 1982 of 3.41, which
20 included both electronic and electromechanical offices. Thus, the
21 report rate in the electromechanical offices is lower, not higher, than
22 it was ten years ago. This reduction has been accomplished at the same
23 time expenses have been cut. Ten years ago an electromechanical office

1 was given routine maintenance on a scheduled basis where each switch and
2 relay was checked for wear and proper adjustment. Today, new technology
3 has been developed which places test calls through these offices during
4 off-peak hours and identifies specific pieces of equipment which are
5 marginal. Central office technicians are then dispatched to repair only
6 those pieces of equipment which are marginal rather than manually
7 testing each piece of equipment as in the past. As a result,
8 maintenance costs in electromechanical offices have also been reduced.
9 Even though it is somewhat more expensive to maintain electromechanical
10 offices than digital offices, in most cases the cost difference are not
11 significant when factored into economic replacement studies.

12 I am proud of the service we are providing throughout the state of Utah,
13 including our electromechanical offices. The electromechanical offices
14 are being adequately maintained and as a result report rates are lower
15 than they were ten years ago. The 2.86 report rate for
16 electromechanical offices, while higher than electronic, is not an
17 indication of inadequate service. It falls well within any reasonable
18 range of good service.

19 Q. MR. DUNKEL AGAIN RAISES THE ISSUE OF INTERCHANGEABLE CODES BY STATING
20 THAT, "THE STEP BY STEP OFFICES WILL NOT WORK WELL WITH THE TOLL SYSTEM
21 WHICH WILL EXIST AFTER JULY 1, 1995." (DUNKEL REBUTTAL, PAGE 53) PLEASE
22 RESPOND.

1 A. As explained in much more detail on pages 22 - 24 of my rebuttal
2 testimony, Mr. Dunkel's conclusion regarding the effect of
3 interchangeable codes are wrong. This issue is totally irrelevant to
4 the central office upgrade issue.

5
6 Q. MR. DUNKEL STATES THAT "THE EXPENSE SAVINGS AND ADDITIONAL REVENUES
7 WHICH ARE AVAILABLE FROM DIGITAL CENTRAL OFFICES FULLY OFFSET THE COST
8 OF REPLACING ELECTROMECHANICAL SWITCHING EQUIPMENT WITH DIGITAL
9 SWITCHING EQUIPMENT." (DUNKEL REBUTTAL, PAGE 16) AND THAT "THE REDUCTION
10 OF EXPENSES AND THE ADDITIONAL REVENUES MORE THAN OFFSET THE HIGHER
11 CAPITAL COSTS FOR 'ECONOMIC REPLACEMENTS'." (DUNKEL REBUTTAL, PAGE 22)
12 PLEASE RESPOND TO THESE STATEMENTS.

13 A. Mr. Dunkel again over-generalizes. In some situations this is true, and
14 in other situations this is not true. I discussed this in detail on
15 page 27 of my rebuttal testimony.

16 It appears that Mr. Dunkel bases his conclusions primarily upon USWC
17 data responses. When USWC first responded to the Committee data
18 requests CCS 2.15 and CCS 10.1, we were not able to provide all of the
19 information that the Committee was requesting. The original response to
20 CCS 2.15 provided the only cost analysis information available on the
21 office modernizations. This information was provided from an analysis
22 done in 1988. This analysis was done on a larger list of offices than
23 the list of offices contained in USWC's Incentive Plan. As explained in
24 the response to CCS 10.1, the revenues were only available in the

1 aggregate. No analyses of revenue had been done on an office-specific
2 basis. Further, as the response to CCS 10.1 explained, a special study
3 would be required to determine what portion of the previous revenue
4 estimate might apply to the current proposal or to develop new revenue
5 estimates that would apply to the current proposal. In response to
6 continued interest expressed in testimonies and interrogatories filed
7 since the Plan was filed (including CCS 14.1, which requested the
8 revenue portion of the study), the Company attempted to obtain the
9 desired information. USWC attempted the aforementioned "special study",
10 starting with the information already available from the 1988 study.
11 The effort consisted of prorating the aggregate revenue amounts to the
12 offices according to the number of lines served by each office. The
13 results were provided in response to CCS 14.1, though they were still
14 based on 1988 data, and further, were limited by the broad-brush method
15 of spreading aggregate revenues by the number of lines. This "special
16 study" showed that only three of the offices (other than replacements
17 scheduled for 1991) would be economical, 19 would be only marginally
18 economical, and the remaining 19 would be uneconomical. However, USWC's
19 overall proposal to upgrade the offices was estimated to be marginally
20 economical though -- without incentive regulation -- clearly suboptimal.

21 Due to the continued attention focused on these economic issues, the
22 Company decided to perform a current study that would be directly
23 applicable to the proposed central office modernizations, without
24 requiring the modifications and adjustments that the older, broader
25 analysis results required. *when*

1 Our Network Planning Department conducted a specific study of the 41
2 electromechanical offices still tied to the USWC's Incentive Plan. The
3 study was finalized at the beginning of this week. USWC has updated the
4 response to CCS 2.15 to reflect the results of this study. The results
5 of this study show that, as a group, the office modernizations would be
6 uneconomical. However, even if the study would have shown that the
7 offices were economical, this would not change the nature of these
8 projects. They are discretionary, and therefore, in a business-as-usual
9 environment, they must compete with other discretionary projects for
10 funding. I explained the process of selecting and funding discretionary
11 projects in detail in my rebuttal testimony.

12 Q. WHY DID USWC DECIDE TO UNDERTAKE A NEW ECONOMIC STUDY OF THE
13 MODERNIZATION OF THE REMAINING ELECTROMECHANICAL OFFICES?

14 A. USWC wanted to be more responsive to the Committee's data requests.
15 Without doing an office-specific study, this would not have been
16 possible. The original information provided to the Committee's data
17 request was based on information gathered during 1988. It included the
18 economic analysis of over 50 offices, and as stated earlier, the
19 revenues were not office-specific. In order to give the Committee the
20 office-specific revenue information that was requested, the revenue was
21 prorated by access lines.

1 The current study looks at the 41 electromechanical offices that remain
2 tied to USWC's Incentive Plan. As a result, USWC is now able to provide
3 more realistic office specific revenue information.

4 Also, many of the assumptions in the 1988 analysis were clearly outdated
5 and needed to be changed.

6 Q. PLEASE EXPLAIN THE RESULTS OF THE NEW ECONOMIC STUDY.

7 A. The results of the study show that, as a group, it is uneconomical to
8 modernize the electromechanical offices. Proprietary Exhibit 1 is the
9 Executive Summary of the Capital Utilization Criteria (CUCRIT) study.
10 In this exhibit, the proposed central office modernization proposal is
11 called "Mod" and the Present Method of Operation (PMO), which would be
12 to continue with the electromechanical offices, is called "Cont PMO"
13 (for "continue PMO").

14 The primary evaluators of the study are Net Present Value (NPV) - End of
15 Study (EOS) and Net Present Worth of Expenditures (NPWE).

16 NPV is a long term after-tax evaluation and is defined as the sum of the
17 present worth of the net cash flow's discounted at the cost of money.

18 For analysis purposes, the NPV should be as large a positive number as
19 possible. A negative NPV would indicate an uneconomical project. NPV
20 answers the question: If the "Mod" project is undertaken, how much
21 advantage will it provide over the life of the project -- in terms of

1 today's dollars -- as compared to the PMO alternative? The negative NPV
2 shows that the proposed "Mod" plan is not economical by the amount
3 indicated -- in today's dollars. Specifically, in this case,
4 implementing the "Mod" alternative would result in the negative number
shown in Proprietary Exhibit 1. Therefore, the "Mod" alternative is
less economical than the "Cont PMO" alternative.

NPWE is the present worth of before-tax revenues required to support a
particular project at the cost of money over and above those revenues
reported by the project. NPWE is a pre-tax cumulative value of all
discounted cash flows. For purposes of analysis, the NPWE should be as
large a negative number as possible. A positive NPWE would indicate an
uneconomical project. NPWE is redundant to NPV insofar as it always
indicates the same thing about whether an alternative is economical or
not. But the NPWE provides additional information because, as a pre-tax
number, it estimates the impact on the Company's revenue requirement of
implementing the "Mod" alternative. Thus, in agreement with the NPV
number, the positive NPWE number shown in Proprietary Exhibit 1
indicates that the proposed modernization plan is not economical. In
this case, the NPWE number in Proprietary Exhibit 1 indicates that the
revenue requirement would increase by approximately that amount over the
life of the study (expressed as a lump sum in today's dollars).

1 Proprietary Exhibit 2 shows the results of the study at the "cluster"
2 level. The "Mod" plan was grouped together in clusters. Because of the
3 digital host-remote technology this is a much more economically viable
4 alternative in comparison to having all stand-alone offices. This
5 exhibit shows how the offices were grouped together in clusters for the
6 study. Because the proposed central office replacements will be done in
7 host-remote combinations according to the cluster arrangements, no
8 cluster can be upgraded without its host office also being upgraded. In
9 three cases (Ogden Main, Park City, and Springville), host offices are
10 identified which are not on the list of proposed central office
11 upgrades, because those host offices have already been upgraded.
12 However, additional investment is required in those offices to support
13 the remote offices in their clusters.

14 Only three of the eight clusters, involving nine of the 41 offices are
15 economical to upgrade as a group. The three clusters are the Logan,
16 Park City, and Vernal clusters. In Proprietary Exhibit 2, in the
17 "Cluster Diff." column, each of these three clusters have a negative
18 NPWE, which indicates that they are economical. The five other clusters
19 have a positive NPWE which indicates that they are uneconomical. The
20 total positive NPWE at the bottom of the exhibit indicates that as a
21 group the office modernizations are uneconomical. Even though some of
22 the clusters would be economical, they are still discretionary and must
23 compete for funding in a business-as-usual environment.

1 This means that, even though the three clusters are economical, there
2 may be yet other projects that are even more economical. Such other
3 projects may well provide even greater benefits to customers or,
4 alternatively, be necessary to maintain adequate service.

5 Proprietary Exhibit 3 is a graph comparing the modernization plan to the
6 PMO plan. The PMO plan is represented as line zero at the top of the
7 graph. This graph is an incremental comparison of the modernization
8 plan to the PMO plan. That is why the PMO plan is shown as line zero.
9 This does not mean that there are no expenditures tied to the PMO plan.
10 This graph shows that USWC will experience a much greater negative NPV,
11 and therefore, a much higher revenue requirement during the life of the
12 Incentive Plan. This means that USWC is absorbing a much greater risk
13 for the office modernizations during the time frame of the Incentive
14 Plan, given the fact that USWC cannot file for rate increases to offset
15 the risk.

16 Q. DO YOU FEEL CONFIDENT WITH THE RESULTS OF THIS STUDY?

17 A. Yes. The estimated increased revenues were based on, actual experience
18 with subscribership results from upgrades in other similar offices. The
19 expected expense savings were primarily based upon historical
20 information of similar upgrades. To validate the study, a sensitivity
21 analysis was performed to determine how much change in revenue or
22 expense would have to occur, in order to reach the break even point
23 (i.e. where the alternative plans would be economically equal).

1 Proprietary Exhibit 4 is a graph of the sensitivity analysis of the
2 revenues included with the modernization plan. This graph shows that
3 the modernization plan would have to realize an additional 2.7 times the
4 projected revenue used in the study before the break even point would be
5 achieved.

6 Proprietary Exhibit 5 is a graph of the sensitivity analysis of the
7 expenses included with the modernization plan. This graph shows that
8 the modernization plan would have to realize about an additional 39%
9 reduction in expenses in order for the break even point to be reached.

10 Proprietary Exhibit 6 is a graph of the sensitivity analysis of the
11 expenses included with the PMO plan. This graph shows that the PMO plan
12 would have to realize 130% higher expenses than the expenses currently
13 tied to the PMO plan, before the modernization plan would be
14 economically equal to the PMO plan.

15 Based on the results of the sensitivity analysis, the office
16 modernizations as a group are clearly uneconomical.

17 Q. DOES THIS CHANGE USWC'S POSITION IN REGARD TO MODERNIZING THE OFFICES?

18 A. No. USWC is willing to guarantee the modernization of all remaining
19 electromechanical offices with the acceptance of its Incentive Plan. We
20 do so based on the premise that incentive regulation will offer us
21 greater opportunities and benefits. In that context, we are willing to

1 commit the capital to change out these offices even though they are
2 uneconomical and will cause a loss for the foreseeable future. During
3 the life of the Incentive Plan, we will not seek rate increases to
4 offset these shortfalls. If an acceptable incentive regulation plan is
5 not approved, then it is only appropriate that we continue on a
6 business-as-usual basis.

7 The Committee's position on office modernization without incentive
8 regulation is internally inconsistent. On one hand, the Committee wants
9 the Commission to reject incentive regulation and continue a regulation-
10 as-usual approach; on the other hand, it wants the Commission to order
11 USWC to abandon a business-as-usual approach when it comes to making its
12 investment decisions. If other parties want USWC to do the office
13 modernization and modify its business-as-usual approach to making its
14 investments, it is only consistent that regulation-as-usual also be
15 modified.

16 Q MR. DUNKEL STATES: "THE COMPANY HAS NOW ADMITTED THAT REPLACEMENT OF THE
17 ELECTROMECHANICAL OFFICES WITH THE DIGITAL CENTRAL OFFICES IS
18 ECONOMICAL, AS IS SHOWN ON SCHEDULE CCS2R-1." (DUNKEL REBUTTAL, PAGE 22)
19 PLEASE RESPOND.

20 A An underlying premise of Mr. Dunkel's statement is that the Company had
21 been taking the position that the office replacements were uneconomical.
22 In fact, before the Committee's data requests, USWC had not classified
23 the office modernization as either uneconomical or economical. The

1 reason is that USWC had not done a specific study in order to determine
2 the economics of the specific office modernizations. USWC was
3 monitoring all electromechanical offices. However, only when a "hard
4 trigger" developed, was an economic study undertaken. The decision of
5 USWC to include the central office upgrades in the Incentive Plan was
6 not based on economics. We had a general indication from the earlier
7 broad brush office analyses that the upgrades were not a clear economic
8 winner over other discretionary projects. Our view was that, in the
9 improved environment of a new form of regulation, we would be willing to
10 commit the capital to do these upgrades, despite the fact that from a
11 traditional perspective they were marginal, at best. Now, other parties
12 are making economics the issue. Given that fact, we have performed a
13 study that shows that these upgrades are not economical. We therefore
14 stand by our basic position. Under incentive regulation, we will make
15 the upgrades. Under traditional regulation, it would be inappropriate
16 to require them to be upgraded because service in those offices continue
17 to be adequate.

18 Q. ON PAGE 33 OF HIS REBUTTAL TESTIMONY, MR. DUNKEL STATES: "A SIGNIFICANT
19 PORTION OF THE FUTURE REVENUE GROWTH IN UTAH WILL NOT BE BECAUSE OF
20 USWC'S UNUSUAL EFFICIENCY, OR USWC'S UNUSUAL PROMOTION OF SERVICES.
21 MUCH OF THE REVENUE GROWTH WILL BE A NATURAL RESULT OF THE GROWTH OF THE
22 NUMBER OF CUSTOMERS. THE ALTERNATIVE REGULATION PLANS WOULD AWARD TO
23 THE SHAREHOLDERS THE MAJORITY OF THE INCREASED PROFITS WHICH WERE CAUSED
24 BY THE GROWTH IN THE NUMBER OF CUSTOMERS." PLEASE RESPOND TO THIS
25 STATEMENT.

1 A. Mr. Dunkel's claim that profits will increase because of customer growth
2 assumes that there are adequate spare facilities available to handle the
3 growth. In some cases there may be adequate spare, in others there
4 clearly will not. Whether the company realizes profits from growth
5 depends upon where the growth materializes and what costs are triggered
6 to support this growth.

7 For example, the Committee of Consumer Services recently has expressed
8 an interest in having telephone service provided to about six customers
9 in the Paria area, which is located between Kanab and Page Arizona near
10 the Utah/Arizona border. These customers reside over eight miles from
11 the Page exchange boundary. The total cost to provide service to these
12 customers would be well over \$130,000. Because these customers reside
13 outside of the exchange boundary, they would be required to pay for 100%
14 of the costs beyond the exchange boundary. We understand that the
15 Committee is considering a petition to have the exchange boundary
16 extended to include these customers. By extending the boundary, these
17 customers would have to pay about \$12,000 instead of \$130,000 for
18 telephone service. If the Commission were to order USWC to extend the
19 exchange boundaries, the increased revenues from these customers will
20 obviously not result in increase profits for USWC.

21 The fact that most growth will not occur in the kind of situation
22 described above, however, does not invalidate this argument. Even in
23 the metropolitan areas, growth can trigger major expenditures. As

1 demonstrated in the last rate case, research by the Division indicated
2 that the utilization in Utah is high. There is little spare capacity,
3 as evidenced by the fact that as access lines have grown since 1988, so
4 has the level of held orders. If USWC did have adequate spare capacity,
5 then the level of held orders would not have grown. Currently, USWC in
6 Utah has the highest utilization outside plant feeder facilities among
7 the 14 states in USWC territory. Because we have high utilization, this
8 means that additional growth cannot continue to be handled with spare
9 facilities. We experienced varying but steady growth in Utah for many
10 years. Yet, until three years ago, we consistently earned below our
11 authorized return. Therefore, history proves that it is wrong to
12 generalize and assume that growth will always lead to increased profits.

13 Q. MR. DUNKEL CONCLUDES THAT USWC IS ASKING FOR A REWARD FOR DOING THE
14 OFFICE MODERNIZATION WHICH IS NORMAL FOR THE INDUSTRY AT THIS TIME.
15 PLEASE RESPOND TO HIS CONCLUSION.

16 A. Apparently, Mr. Dunkel bases his conclusion upon a report provided by
17 Dr. Davidson. The source of this information is from direct surveys.
18 There are some potential problems with reading too much into the
19 information. For example, this report does not indicate what portion of
20 the "planned" office modernization is based upon "hard triggers", what
21 portion is tied to incentive regulation proposals, and what portion is
22 attributable to other reasons. Any information provided by USWC would
23 have been based upon Fundamental Plans. It is reasonable to assume that
24 other Bell Operating Companies provided the information from similar

1 sources. On page 1 of my rebuttal testimony, I discuss the nature of
2 Fundamental Plans. The Fundamental Plans in most USWC states currently
3 reflect an accelerated office modernization program as a result of
4 incentive regulation proposals.

5 The real issue is not how USWC in Utah compares to other Independents in
6 Utah, or to other telephone companies throughout the nation. The real
7 issue is that USWC's modernization proposal is an accelerated proposal
8 in comparison to a business-as-usual approach, and that without
9 incentive regulation, USWC cannot guarantee the office modernization.

10 Q. ARE THERE ANY OF THE CONCEPTS IN MR. DUNKEL'S REBUTTAL TESTIMONY THAT
11 HAVE MERIT?

12 A Yes, his concept of Universal Service is similar to USWC's concept. USWC
13 is committed to facilitating Universal Service. However, USWC is also
14 committed to balancing the goal of Universal Service with the goal of
15 minimizing costs that are passed on to the general body of ratepayers.

16 RESPONSE TO ISSUES RAISED BY THE COMMISSION AND RESPONSE TO MR. DUNKEL'S
17 DIRECT RATE DESIGN TESTIMONY.

1 Q. THE COMMISSION HAS ASKED USWC TO RESPOND TO THE ISSUE OF WHAT IS DRIVING
2 THE NEED TO REPLACE PLANT FASTER BY STATING: "ONE ASPECT IN PARTICULAR
3 WE SEEK TO BETTER UNDERSTAND CONCERNS CHANGING CUSTOMER DEMANDS,
4 EXISTING AND NEW SERVICE REQUIREMENTS AS THE COMPANY SEES THEM, AND
5 PINPOINTING THE CUSTOMERS BY TYPE THAT ARE BEHIND THE PUSH TO REPLACE
6 PLANT FASTER." (SCHEDULING ORDER, 90-049-03 AND 90-049-06, NOVEMBER 23,
7 1990, PAGE 3) PLEASE RESPOND TO THIS ISSUE.

8 A. Implicit within this question is the assumption that it is possible to
9 specifically pinpoint which customers or services drive technology
10 changes. In reality, the issue is much more complex than that. In most
11 cases, it is a combination of factors, many of which simply cannot be
12 traced to specific customer classes. A combination of customers and
13 services, including basic services, drive technology change.

14 Q. PLEASE EXPLAIN HOW THIS OCCURS?

15 A. When a decision is made to make a technology upgrade, there is usually a
16 trigger driving USWC to that decision. Often the trigger is basic
17 service growth. In an economic study, the present method of operations
18 (PMO) is compared to other alternatives. If a "hard trigger" developed
19 in an electromechanical office, the PMO would be to continue to
20 reinforce with electromechanical equipment. The alternative to PMO
21 would be to modernize with digital technology. When the study is
22 performed, projected incremental revenues resulting from new services is
23 included with the modernization alternative. These projected
24 incremental revenues usually come from both residential and business

1 customers being able to buy services that cannot be offered with the
2 existing technology. At the same time, incremental expenses are also
3 included in the study. For example, the higher maintenance costs of the
4 electromechanical office switch would also be included in the study.
5 Maintenance costs include the repair costs for both residential and
6 business customers. Also, other costs, like building additions,
7 rearrangement costs, analog to digital conversion costs, etc. would be
8 included in the study. In some situations, the building addition costs
9 alone make the modernization alternative an economic winner. Often a
10 digital remote or stand alone switch can be placed in available space
11 too small to accommodate electromechanical expansion. Placing the
12 digital switch thus eliminates the need for a costly building addition.

13 In an effort to ensure the validity in the study, we try to capture all
14 relevant costs and revenues so that the best economic decision can be
15 made.

16 Given the myriad factors that impact such decisions, it would be
17 inappropriate to generalize and assume that one particular factor or
18 service category is the major reason that the modernization alternative
19 is selected. The only time this should be claimed is in situations
20 where one factor really makes the difference. Such cases are the
21 exception, not the rule.

1 Q. IN HIS DIRECT RATE SPREAD TESTIMONY, MR. DUNKEL STATED THAT "THE PRIMARY
2 CAUSE OF THE MORE RAPID REPLACEMENT OF EQUIPMENT . . . ARE FOR THE
3 PROVISION OF NON-BASIC SERVICES." (PAGE 48) IS HIS STATEMENT CORRECT?

4 A. No. While he makes the statement, he provides virtually no factual
5 support for it. Mr Dunkel uses the Ogden North central office
6 replacement as an example to support his erroneous conclusion. The
7 Ogden North central office, which was recently replaced with a digital
8 switch, is actually a clear illustration of how a combination of factors
9 leads to the decision to deploy new technology. In using the Ogden
10 North example, Mr. Dunkel quoted selective information from the study,
11 while totally ignoring other important information. For example, after
12 quoting one portion of the Company analysis of the North Ogden
13 replacement, Mr. Dunkel stated that "the availability of the premium
14 services available from a digital switch was one of the major goals of
15 these replacements." (Dunkel, Direct Rate Spread Testimony, page 54)
16 What he totally fails to mention is the "hard trigger" for that project,
17 which was the forecasted exhaust of available central office equipment
18 in May 1990. In other words, the immediate reason for the switch
19 replacement was because of the exhaust of central office capacity, which
20 has absolutely nothing whatsoever to do with the offering of premium
21 services. It had to be replaced to meet the demand for basic residence
22 and business services. In fact, given the fact the Ogden North wire
23 center is located in a bedroom community, basic residential service
24 growth was the primary driving factor. This is clearly shown by the
25 fact that approximately 90% of the access lines in this wire center are
26 residential access lines.

1 When the economic study of the Ogden North office was performed, all
2 relevant factors were included in the analysis. The projected revenue
3 from vertical services was one of the many factors included in the
4 study. Contrary to what Mr. Dunkel implies, this factor alone did not
5 make the digital office alternative the most economical. In fact, the
6 Ogden North digital office would have still been the most economical
7 alternative, even if the additional revenues from vertical services
8 would have been excluded from the study, as shown in Proprietary
9 Exhibit 7. The proprietary number that Mr. Dunkel used from the study
10 in his rebuttal testimony was the total non-discounted revenue over the
11 life of the study. Proprietary Exhibit 7 shows the net present worth of
12 this revenue, and shows that even if the revenue from vertical services
13 had been excluded from the study, the digital modernization alternative
14 would have still been the most economical alternative by about
15 \$500,000 (NPWE).

16 Q. ARE THERE OTHER EXAMPLES OF MODERNIZATION BEING TRIGGERED BY GROWTH OF
17 BASIC SERVICE?

18 A. Yes. The Payson office modernization, which is planned for this year,
19 is a good example. The need to change technology is being triggered by
20 the exhaust of the remaining spare capacity in the line equipment.
21 There is not enough space in the building for a step-by-step addition.
22 However, there is enough space for a digital remote switch. The
23 expenses of continuing PMO in this particular situation is another major
24 factor driving the replacement of the Payson office. All of the

1 factors combined, including the projected revenues from vertical
2 services makes the modernization plan an economic winner over the PMO
3 plan. But, even without the incremental revenues, it is an economical
4 decision to replace the central office.

5
6 The Lehi office modernization is another example of the same situation.
7 Given that both Payson and Lehi are predominately residential
8 communities, the need to do something is clearly being triggered
9 primarily by the growth of residential basic service. In Payson, 83% of
10 the existing access lines are residential lines; in Lehi, 87% of the
11 existing access lines are residential lines.

12 Q. ARE THERE OTHER SITUATIONS BESIDES CENTRAL OFFICE REPLACEMENTS, WHERE A
13 COMBINATION OF FACTORS OR SERVICES LEADS TO MODERNIZATION?

14 A. Yes. This combination of factors drive the modernization of the outside
15 plant as well. During the last rate case, Roger Weaver analyzed USWC's
16 fiber projects. His conclusion regarding nine of the fiber projects
17 was that "the selection of fiber over copper to meet expanding service
18 requirements in these existing routes is a straight forward selection of
19 the most economical alternative." (Weaver Direct, Case No. 88-049-07,
20 page 4) The need for these outside plant feeder relief projects was
21 triggered by the growth of a combination of several services including
22 basic and special services. Projected revenues for vertical services
23 such as custom calling features had no impact on these projects, because
24 these services can be provided on either copper or fiber. In fact, all

1 of the services included in the study could be provided on copper or
2 fiber. However, cost savings could be realized by using fiber. The
3 savings in provisioning costs was one of the many factors that lead to
4 the economic selection of fiber.

5 Dr. Weaver also evaluated seven fiber projects that were done for
6 specific customers. In relation to these projects, he concluded that
7 "These projects were undertaken to meet specific requests of the
8 identified contracting customer. Their costs are paid for by the
9 customer directly and are not included in any aspect of the ratemaking
10 process for the general body of ratepayers at either the state or the
11 federal level." (Weaver Direct, Case No. 88-049-07, page 17) Therefore,
12 when specific customers trigger specific modernization jobs, these
13 customers pay for the service being provided to them.

14 Also, in almost all situations, when digital line carrier is used to
15 reinforce the outside feeder network, it is selected because it is the
16 most economical alternative. Given that the digital line carrier proves
17 to be more economical than the copper alternative at farther distances
18 from the central office, many times it is residential growth that is
19 triggering the modernization.

20 Q. ARE THERE SITUATIONS WHERE VERTICAL SERVICES DRIVE THE DECISION TO
21 SELECT NEW TECHNOLOGY?

1 A. There are some situations where vertical services become primary factors
2 in making the modernization alternative an economic winner. For
3 example, the results of the recent study involving the 41
4 electromechanical offices tied to the USWC Incentive Plan showed that
5 three of the eight clusters were economical. As shown in Proprietary
6 Exhibit 2, if the projected revenues included in the study were removed,
7 the three economical clusters would become uneconomical. In this
8 particular situation, the projected revenues from vertical services
9 contributes to make three of the eight clusters economical. However,
10 there are several other important factors that also contribute.
11 Therefore, it is not appropriate to overgeneralize and assume that
12 either vertical services or any particular group of customers is driving
13 the need to modernize the plant.

14 It should be noted that in almost all of the examples cited, the
15 majority of the revenue from vertical services is revenue generated by
16 residential customers, and not business customers.

17 In general, because of the significant margins realized with vertical
18 services, customers who subscribe to these services help keep basic
19 service rates low.

20 Q. MR. DUNKEL ARGUES THAT DEPRECIATION EXPENSE SHOULD SOMEHOW BE ALLOCATED
21 TO SERVICES OTHER THAN BASIC SERVICE BASED ON HIS VIEW THAT BASIC
22 SERVICE DOES NOT DRIVE THE DEPLOYMENT OF NEW TECHNOLOGY. PLEASE
23 RESPOND.

1 A. I have demonstrated that the factual premise of Mr. Dunkel's argument is
2 false. Each capital deployment decision, whether a CO upgrade, a feeder
3 addition, or a distribution placement, is based on a variety of factors
4 including basic service growth. Growth in basic service is a major
5 factor in most technology deployments. In some cases, it is the only
6 factor. Thus, there is no factual reason to do what Mr. Dunkel
 proposes.

7 While I am not an expert in cost studies and allocations, even if it
8 were factually supportable, I cannot imagine how depreciation would be
9 allocated. Mr. Dunkel's ambiguous proposal has provided us with no
10 guidelines. In my view, it would be a massive and ultimately fruitless
11 task to attempt to reallocate depreciation as Mr. Dunkel proposes. It
12 would necessitate a separate analysis of each capital deployment
13 decision and an allocation of depreciation different in each case. Such
14 an approach would not be realistic or worthwhile.

15 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

16 A. Yes.

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NETWORK PLANNING SYSTEM

* EXECUTIVE SUMMARY *

RESULTS IN THOUSANDS (\$000)

TSR-1

STUDY: Utah Rural Mod Restudy 1991
PARAMETER FILE:

PLAN: MOD (92-96) VS Cont PMO

++++++ INCREMENTAL CASH FLOW ECONOMIC EVALUATORS ++++++

	PRIMARY	
NET PRESENT VALUE - EOS	-7708.1	←
NET PW EXPENDITURES	12313.3	←
	SECONDARY	
CUMULATIVE DISCOUNTED CASH FLOW AT END OF LIFE	-7708.1	
DISCOUNTED PAYBACK PERIOD	NO PAYBACK	
LONG TERM ECONOMIC EVALUATOR	0.601	
INTERNAL RATE OF RETURN	6.6%	

++++++ INCREMENTAL SHORT TERM FINANCIAL MEASURES ++++++

YEAR	NET INCOME	NET AVG INV CAP	RETURN ON NAIC (%)	EQUITY AVG INV CAP	RETURN ON EQAIC (%)
1990	-0.1	0.8	-4.4	0.5	-13.8
1991	-32.5	227.7	-10.4	136.6	-23.8
1992	-181.4	31224.3	3.3	18734.6	-1.0
1993	-682.9	48221.0	2.5	28932.6	-2.4
1994	-625.1	53016.7	2.7	31810.0	-2.0

++++++ SUMMARY BY PLAN ++++++
MOD (92-96)

	MOD (92-96)	Cont PMO
TOTAL NONDISCOUNTED CAP.	74576.2	53001.2
TOTAL NONDISCOUNTED EXP.	107535.4	137384.8
TOTAL NONDISCOUNTED REV.	30159.6	0.
NET PRESENT VALUE-EOS	-45877.8	-38169.8
NET PW EXPENDITURES	73287.7	60974.4

++++++ STUDY PARAMETERS AND FOOTNOTES ++++++

PRESENT WORTH YEAR 1990	TREND BASE DATE 1/1990	CASH FLOW OPTION COME
LENGTH OF STUDY 20 YEARS	DISC RATE 12.30%	FINANCIAL OPTION ACCT

CUCRIT IS NORMALLY USED TO PERFORM AN INCREMENTAL ANALYSIS. THUS THE EVALUATORS MEASURE THE DIFFERENCE IN THE VALUE OF THE TWO PLANS, NOT THE ABSOLUTE VALUE OF EITHER PLAN.

UTAH ELECTROMECHANICAL OFFICE REPLACEMENT STUDY - 1991
NET PRESENT WORTH of EXPENDITURES (\$,000)

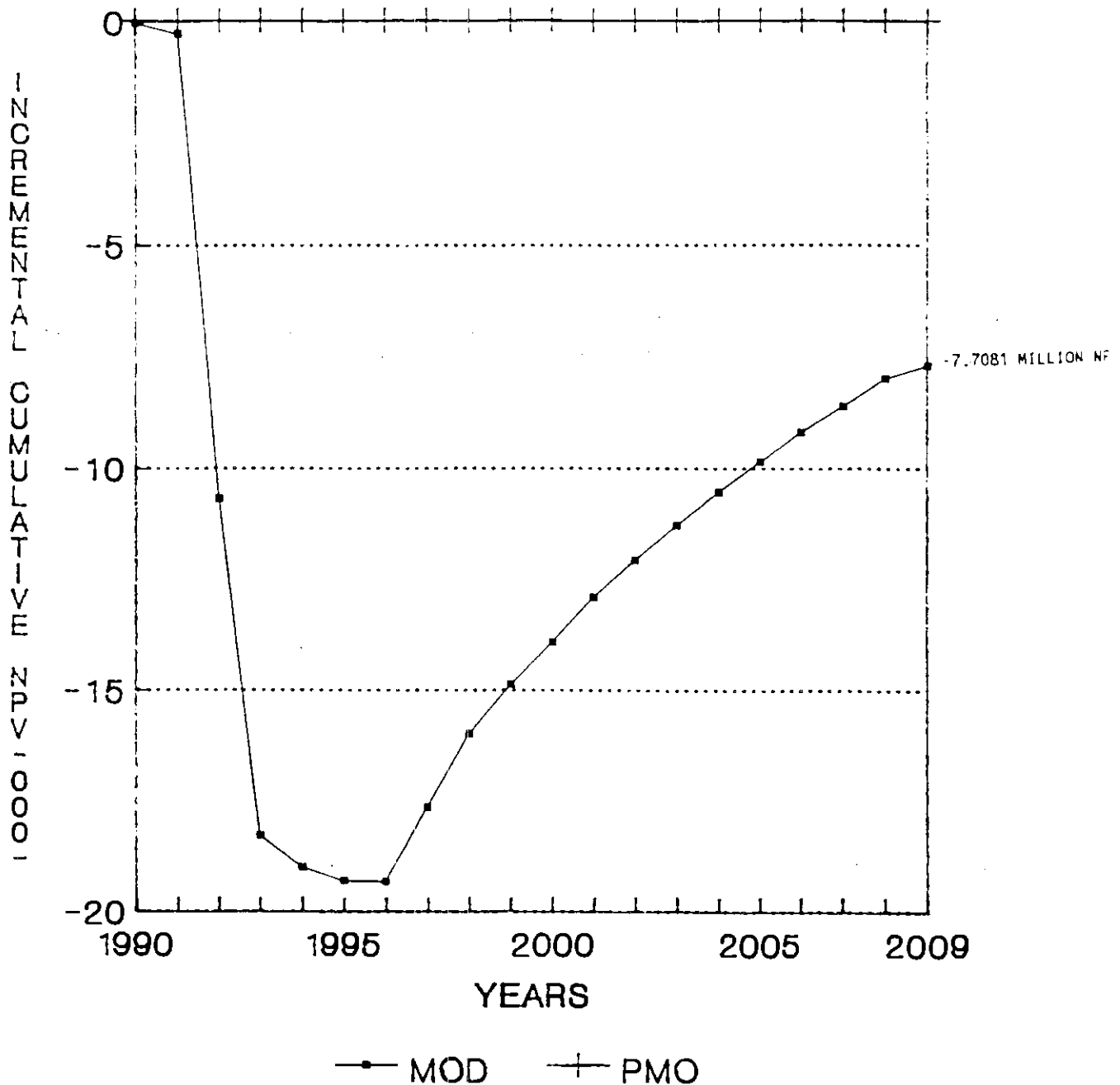
PROPRIETARY EXHIBIT 2
P.S. SELANDER

75R.2

OFFICE	DATE	(A) "PMO"	(B) "Mod"	Diff. (B)-(A)	% Diff.	Cluster Diff.	% Diff.	Revenue	Cluster Revenue	Cluster Diff. w/o Revenue	% Diff.
CEDAR CITY (Host)	Jun-93	\$4,572.1	\$6,575.8	\$2,003.7	43.8%			\$0.0			
PAROWAN	Jul-93	712.4	1,243.8	531.4	74.6%			\$158.5			
BEAVER	Aug-93	1,647.8	1,501.7	(146.1)	-8.9%			\$167.8			
MILFORD	Sep-93	1,555.4	1,681.8	126.4	8.1%			\$73.4			
ENTERPRISE	Oct-93	236.0	370.8	134.8	57.1%			\$46.9			
MINERSVILLE	Oct-93	256.8	974.3	717.5	279.4%			\$37.7			
PANGUITCH	Sep-94	755.1	2,295.5	1,540.4	204.0%			\$146.3			
BRUCE CANYON	Sep-94	185.1	1,156.8	971.7	525.0%			\$18.6			
HATCH	Sep-94	192.6	1,115.6	923.0	479.2%			\$19.5			
SPRINGDALE	Jun-95	530.7	399.7	(131.0)	-24.7%			\$68.6			
VEYO	Jun-95	769.1	496.1	(273.0)	-35.5%			\$116.3			
LEEDS	Jun-95	359.9	327.2	(32.7)	-9.1%	\$6,366.1	54.1%	\$37.0	\$890.6	\$7,256.7	61.6%
LOGAN (Host)	Jun-92	6,076.7	7,292.8	1,216.1	20.0%			\$0.0			
RICHMOND	Jun-92	762.0	513.5	(248.5)	-32.6%			\$183.6			
SMITHFIELD	Jun-93	1,596.5	884.2	(712.3)	-44.6%			\$417.3			
HYRUM	Jun-93	1,866.1	1,510.8	(355.3)	-19.0%			\$407.2			
GARDEN CITY	Oct-94	2,850.3	2,458.3	(392.0)	-13.8%	(492.0)	-3.7%	\$136.7	\$1,144.8	\$652.8	5.0%
OGDEN (Host)	Dec-92	7,933.2	7,953.0	19.8	0.2%			\$0.0			
MORGAN	Dec-92	676.1	2,586.4	1,910.3	282.5%			\$174.9			
MTN. GREEN	Dec-92	430.1	532.5	102.4	23.8%	2,032.5	22.5%	\$85.2	\$260.1	\$2,292.6	25.4%
PARK CITY (Host)	Aug-90	3,561.6	3,747.9	186.3	5.2%			\$0.0			
HEBER CITY	Jul-92	2,680.7	1,564.4	(1,116.3)	-41.6%			\$619.9			
COALVILLE	Aug-93	632.4	1,293.2	660.8	104.5%	(269.2)	-3.9%	\$164.0	\$783.9	\$514.7	7.5%
PRICE (Host)	Nov-92	3,732.5	2,970.4	(762.1)	-20.4%			\$924.6			
HELPER	Dec-93	767.6	756.9	(10.7)	-1.4%			\$161.0			
EAST CARBON	Jul-96	281.6	379.3	97.7	34.7%			\$57.6			
HUNTINGTON	Sep-96	685.4	1,148.7	463.3	67.6%			\$71.8			
GREEN RIVER	Oct-96	356.7	389.1	32.4	9.1%			\$65.4			
HIWATHA	Nov-96	96.1	398.4	302.3	314.6%			\$2.4			
SCOTFIELD	Dec-96	258.6	1,856.5	1,597.9	617.9%	1,720.8	27.9%	\$18.9	\$1,301.7	\$3,022.5	48.9%
RICHFIELD (Host)	Nov-93	2,052.1	2,580.1	528.0	25.7%			\$480.9			
SALINA	Nov-94	1,047.6	1,433.5	385.9	36.8%			\$202.4			
MONROE	Dec-94	714.6	1,326.0	611.4	85.6%			\$143.7			
BICKNELL	Jul-95	734.8	577.7	(157.1)	-21.4%			\$94.7			
LOA	Aug-95	1,540.1	1,483.9	(56.2)	-3.6%			\$70.6			
HANKSVILLE	Sep-95	151.2	447.6	296.4	196.0%			\$15.1			
CIRCLEVILLE	Oct-95	456.6	1,229.3	772.7	169.2%			\$61.9			
MARYSVALE	Nov-95	271.9	305.1	33.2	12.2%	2,414.3	34.6%	\$35.3	\$1,104.6	\$3,518.9	50.5%
SPRINGVILLE (Host)	Sep-91	2,072.5	2,132.8	60.3	2.9%			\$0.0			
MT. PLEASANT	Jul-94	775.2	609.7	(165.5)	-21.3%			\$168.0			
EPHRAIM	Jul-94	813.0	684.2	(128.8)	-15.8%			\$153.0			
GOSHEN	Aug-94	213.6	1,329.3	1,115.7	522.3%			\$35.2			
EUREKA	Aug-94	319.1	449.8	130.7	41.0%	1,012.4	24.1%	\$46.8	\$403.0	\$1,415.4	33.8%
VERNAL (Host)	Oct-92	2,509.4	2,844.6	335.2	13.4%			\$942.4			
ROOSEVELT	Oct-92	1,435.4	809.8	(625.6)	-43.6%			\$433.8			
DUCHESNE	Oct-92	428.8	461.8	33.0	7.7%	(257.4)	-5.9%	\$111.4	\$1,487.6	\$1,230.2	28.1%
TOTALS		\$62,553.1	\$75,080.6	\$12,527.5	20.0%	\$12,527.5	20.0%		\$7,376.3	\$19,903.8	31.8%

NOTE: NPWE source from Plan Evaluator - Network Planning System Wirecenter. There is a small difference between Plan Evaluator NPWE and CUCRIT NPWE due to time of the year the investment is booked (CUCRIT - assumes 1st of the year, Plan Evaluator assumes mid-year). A negative number in a Diff. column means that "Mod" plan is an economic winner. The revenue numbers were a deduction to the NPWE of the "Mod" plan. If revenues are to be excluded from the study, then the revenue amount shown must be added back in with the NPWE of the "Mod" plan.

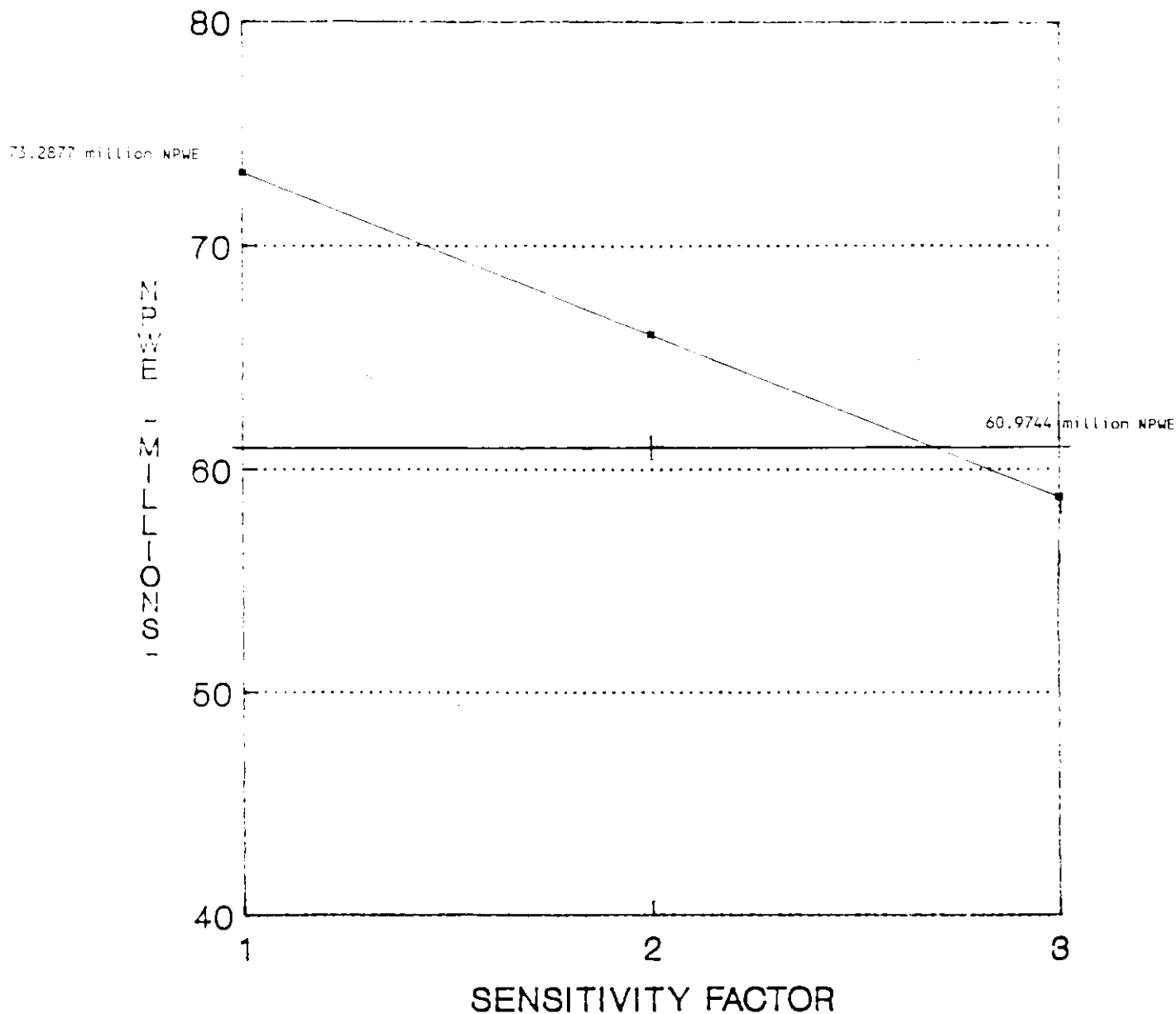
GRAPHICAL COMPARISON OF ALTERNATIVES UTAH RURAL MOD RESTUDY 91



This graph shows the modernization (MOD) alternative in comparison to the PMO alternative. The PMO plan is represented as line zero at the top of the graph. This graph is an incremental comparison of the MOD plan to the PMO plan. That is why PMO is shown as line zero. This does not mean that there are no expenditures tied to the PMO plan. The y-axis numbers are the negative NPV in millions of dollars. The x-axis numbers are the years during the life of the study. Notice at year 2009 the NPV is the same figure as the figure shown in Proprietary Exhibit 1 for the NPV. At year 1996, the NPV of the MOD plan would be about a negative \$19 million.

7824

REVENUE SENSITIVITY UTAH RURAL MOD RESTUDY 91

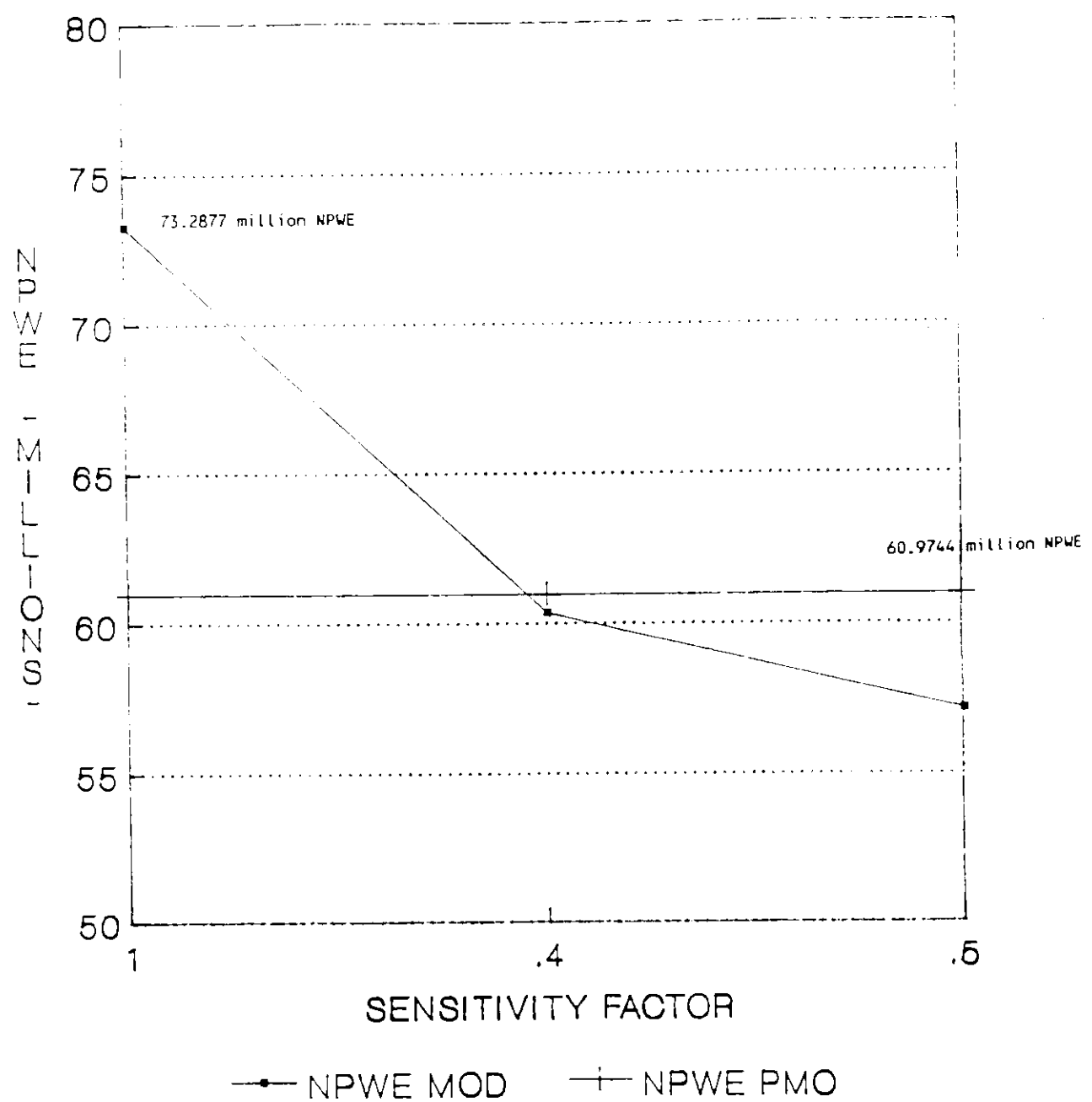


—●— NPWE MOD —+— NPWE PMO

This graph shows the results of the sensitivity analysis of the revenues included with the modernization (MOD) plan. The y-axis numbers are the NPWE numbers in millions of dollars. Notice at the starting point that the 73.2877 million is the same NPWE number as shown under the MOD (92-96) column in Proprietary Exhibit 1. The x-axis numbers represent the sensitivity factors or the number of times that revenue changes. The line in the middle of the graph is the PMO plan. Notice the number 60.9744 million is the same NPWE number as shown under the Cont PMO column in Proprietary Exhibit 1. PMO is held constant and thus is represented as a flat line. This graph shows that the revenue included with the MOD plan would have to increase about 2.7 times (or 270%) before the cross over point. At that point the MOD plan would be equal economically to the PMO plan.

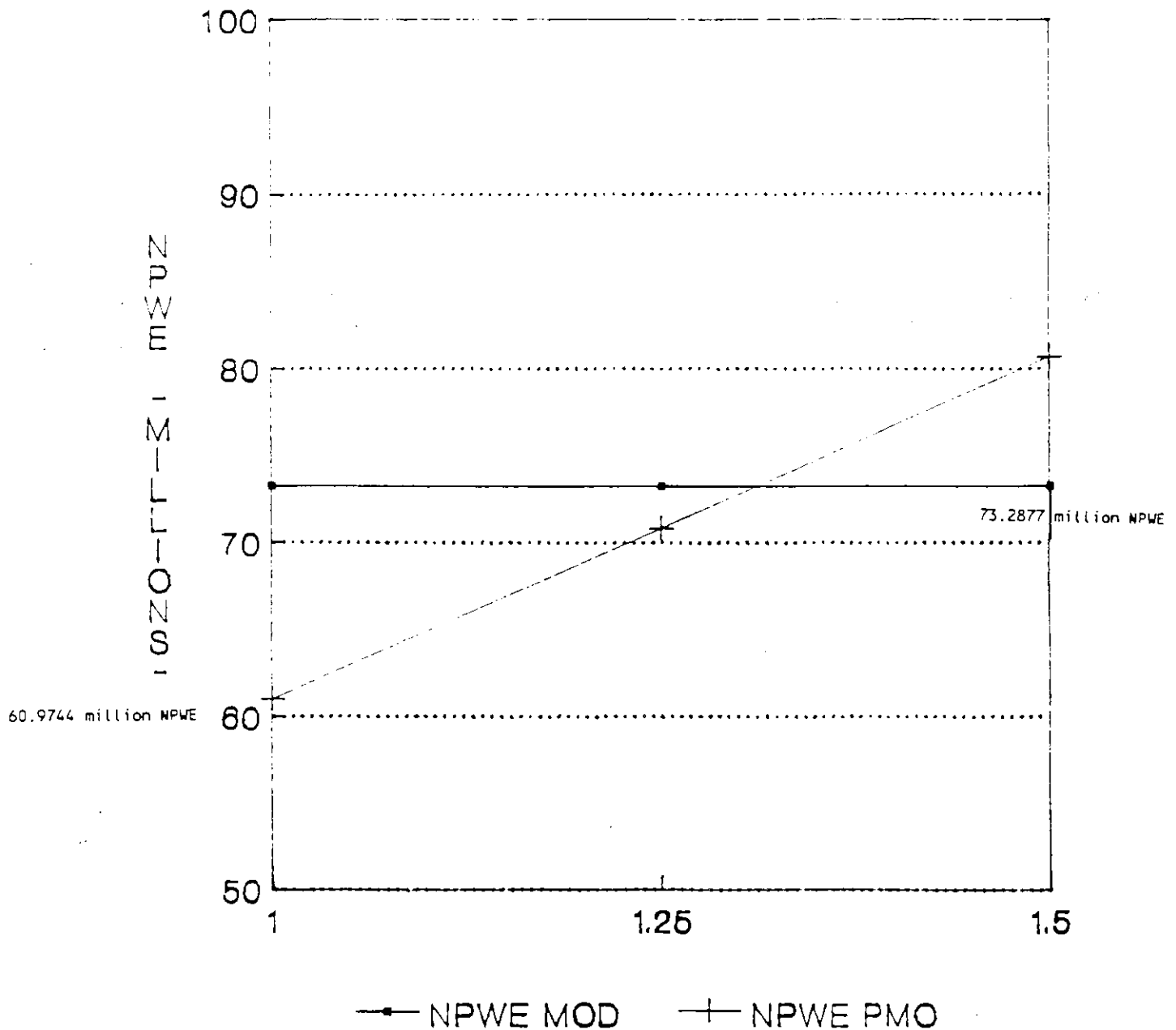
752.5

EXPENSE SENSITIVITY MODERNIZATION



This graph shows the amount that the expenses associated with the modernization (MOD) plan would have to be reduced in order for the MOD plan to reach the cross over point where both plans are equal economically. The y-axis numbers are the NPWE in millions of dollars, and the x-axis numbers represent the sensitivity factors. The PMO plan is held constant and thus is represented as a flat line. This graph shows that the expenses of the MOD plan would have to decrease about .39 times or 39% before the cross over point is reached. At this point the MOD plan is equal economically to the PMO plan.

EXPENSE SENSITIVITY PMO



This graph shows the amount that the expenses associated with the PMO plan would have to increase in order for the modernization (MOD) plan to be equal economically to the PMO plan. The y-axis numbers are the NPWE in millions of dollars, and the x-axis numbers represent the factors or number of times expense changes. In this graph the MOD plan is being held constant and is represented by the flat line. This graph shows that the expenses associated with the PMO plan would have to increase about 1.3 times (130%) before both plans would be equal economically.

PROPRIETARY EXHIBIT 7
P.S. SELANDER

OGDEN NORTH CENTRAL OFFICE ECONOMIC NPWE PLAN COMPARISON

With Revenue included in the Study:

	<u>PLAN PMO - GROW X-BAR</u>	<u>PLAN DIGITAL MODERNIZATION</u>
CAPITAL	\$2,825,167	\$3,086,547
EXPENSE	\$1,982,420	\$1,222,033
REVENUE	(\$ 0)	(\$1,124,035)
	-----	-----
TOTAL NPWE	\$4,807,587	\$3,184,545
DIFFERENCE (Digital Plan - PMO)		(\$1,623,042)

With Revenue excluded from the Study:

	<u>PLAN PMO - GROW X-BAR</u>	<u>PLAN DIGITAL MODERNIZATION</u>
CAPITAL	\$2,825,167	\$3,086,547
EXPENSE	\$1,982,420	\$1,222,033
	-----	-----
TOTAL NPWE	\$4,807,587	\$4,308,580
DIFFERENCE (Digital Plan - PMO)		(\$ 499,007)

Note: Information for this exhibit was compiled from Plan Evaluator - Network Planning System Wirecenter. The information for this exhibit was compiled from the same information that was part of the response to CCS 10.6. The \$4.895 million number that Mr. Dunkel refers to in his rebuttal testimony is the total non-discounted revenue over the life of the study. The equivalent NPWE for this number is \$1.124 million. The negative number under Plan Digital Modernization means that this plan is the economic winner.

ADDENDUM E

EXCERPTS FROM THE TRANSCRIPT OF
A HEARING HELD BEFORE THE
UTAH PUBLIC SERVICE COMMISSION

JULY 1, 1991

CONSOLIDATED DOCKET NOS. 90-049-03 &06

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

--oOo--

COPY

In the Matter of the
Application of US West
Communications for Approval
of an Incentive Regulation
Plan.

) Case No. 90-049-03
)
)
)
)
)
)

In the Matter of the
Investigation into the
Reasonableness of its Rates
and Charges for US West
Communications.

) Case No. 90-049-06
)
) REPORTER'S TRANSCRIPT
) OF PROCEEDINGS
)
)

Salt Lake City, Utah

Monday, July 1, 1991

10:00 a.m.

BEFORE:

BRIAN T. (TED) STEWART, Chairman, Public
Service Commission of Utah;

JAMES M. BYRNE, Commissioner, Public
Service Commission of Utah;

STEPHEN MECHAM, Commissioner, Public
Service Commission of Utah.

--oOo--

WENDY K. RANDALL, CSR, RPR
160 E. 300 S. 4th Floor
Salt Lake City, UT 84111
(801) 530-6693

A P P E A R A N C E S

FOR US WEST
COMMUNICATIONS: TED D. SMITH, ESQ.
250 Bell Plaza
Salt Lake City, Utah 84111

FOR THE DIVISION
OF PUBLIC
UTILITIES: MICHAEL GINSBERG, ESQ.
Assistant Attorney General
36 South State, #2200
Salt Lake City, Utah 84114

FOR THE COMMITTEE
OF CONSUMER
SERVICES: KENT WALGREN, ESQ.
Assistant Attorney General
36 South State, #2200
Salt Lake City, Utah 84114

I N D E X

PROCEEDINGS

3 - 78

1 Date: July 1, 1991
2 Time: 10:00 a.m.

3 P R O C E E D I N G S

4 COM. STEWART: Let's go on the record in
5 docket number 90-049-03 in the matter of the
6 application of US West Communications for approval of
7 an incentive regulation plan and docket number
8 90-049-06 in the matter of the investigation into the
9 reasonableness of the rates and charges of US West
10 Communications. We are here today to hear a petition
11 of US West Communications' for delaying the effective
12 date of order or stay. If we could take appearances
13 for the record?

14 MR. SMITH: Ted Smith for US West
15 Communications, Inc.

16 MR. GINSBERG: Michael Ginsberg for the
17 Division of Public Utilities.

18 MR. WALGREN: Kent Walgren, Committee of
19 Consumer Services.

20 COM. STEWART: Mr. Smith, it's your
21 petition. If you would like to proceed.

22 MR. SMITH: Yes, Mr. Chairman. Let me
23 address a few preliminary items, if I could. I have
24 handed out some exhibits that have been entitled,
25 "Exhibits of USWC in Aid of Argument" that we would

1 like to present here and we will use them as part of
2 the argument. It's six pages of material and I will
3 refer to them in the argument.

4 The first item I would like to address is a
5 preliminary matter that I would just like to note for
6 the record, a matter of concern to the Company. It
7 actually relates to the last item in the packet that
8 was handed out that is a news report, I think as of
9 last Wednesday, in the Deseret News regarding the
10 Company's petition.

11 The concern that the Company has that we would
12 like to just note is the last sentence in that report
13 indicates, and it's referring to apparently an
14 interview held between the reporter and Mr. Stott, who
15 is the legal counsel for the Commission. The last
16 statement there is Stott said, "The Commission is
17 satisfied the order is complete and there is no need
18 for a rehearing."

19 We realize that newspapers don't always quote
20 things exactly right and it may be the context isn't
21 entirely clear, but I will just note for the record
22 that it is very troubling to the Company to see a
23 quotation that seems to indicate perhaps that the
24 issues that are being raised here have perhaps been
25 predetermined or indeed the issues that we may raise

1 on the petition for review or rehearing may be
2 predetermined.

3 I would just note that for the record, that that
4 does cause the Company some concern, and we will just
5 leave it at that.

6 One other issue and perhaps this isn't the
7 appropriate time to raise it, but as I have read the
8 order issued by the Commission on June 19th, it
9 appears to me that the portions of the order that are
10 the formal findings of fact or conclusions of law are
11 the portions that are set forth in bold print. I just
12 wanted to ask a general question to the Commission and
13 ask if that indeed is what can be deemed the findings
14 of fact or conclusions of law?

15 COM. STEWART: That is correct. Let me
16 comment if I may just a minute on your newspaper
17 argument. The point of the matter is that I think at
18 any given point in time after the issuance of an order
19 by the Commission, I think it must be assumed that the
20 Commission and the staff, including our counsel, stand
21 by the order. I think that is simply what Mr. Stott
22 was saying, that within a matter of days of issuance
23 of this order, the Commission stands by it. I do not
24 believe in any way Mr. Stott was prejudging the
25 filings that have subsequently come in from the

ADDENDUM F

EXCERPTS FROM THE REPORT AND ORDER
OF THE UTAH PUBLIC SERVICE COMMISSION

OCTOBER 18, 1989

DOCKET NO. 88-049-07

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Investi-)
gation into the Reasonableness of)
the Rates and Charges of THE)
MOUNTAIN STATES TELEPHONE AND)
TELEGRAPH COMPANY.)

DOCKET NO. 88-049-07

REPORT AND ORDER

ISSUED: October 18, 1989

SYNOPSIS

By this Order the Commission: approves a reduction in annual revenue requirement of 6.41 percent, or \$ 21,847,000; resolves a number of accounting issues pertinent to establishing the correct test year information; determines a cost of equity capital of 11.8 percent and a rate of return on rate base or net investment of 10.64 percent; embraces the use of embedded cost-of-service analysis as a major consideration for spreading revenue requirement to service or product categories; reiterates its adherence to standard ratemaking objectives supplemented by pricing principles suggested by the parties and by universal service considerations as the proper guides to ratemaking; establishes the prices or bases for prices of products and service elements provided by the utility; and orders the Company and the Division to conduct further work on various subjects, such work to be completed prior to the next rate case for this Company.

Earlier in this Order, the Commission declined to find that disallowances for rate base utilization were appropriate but indicated concern about certain of the issues the Division raised. We recognize the Company's concern about the difficulty of establishing what amounts to efficiency standards for the provision of utility services. Additionally, we recognize that a potential conflict exists between regulatory objectives concerning the public interest as it applies to basic utility services and company objectives concerning the pursuit of private interest in competitive markets.

We find that plant utilization objectives would be useful in future evaluation by the Division of USWC's plant utilization. Therefore, we will direct the Division to continue its effort to develop plant utilization objectives by discussing these issues further with the Company in the hope of achieving some common ground on which to base further analysis. A Stipulation or the Division's recommendations should be submitted to the Commission by March 1990.

3. ACCELERATED REPLACEMENT OF ALL STEP-BY-STEP CROSS-BAR SWITCHES

USWC continues to employ a number of Step-by-Step and Cross-Bar switches in the State. Because USWC's rate base has been declining during the last two years, the Division contended that this may be an advantageous time for the Commission to consider replacing or upgrading these older switches earlier than might be indicated by their useful lives. The Division asserted that an upgrade now could facilitate the provision of Enhanced 9-1-1 service and custom calling features, and would improve the telecommunications infrastructure in Utah's rural areas. The Division contended that a declining rate

base coupled with accelerated depreciation of older equipment would permit such an upgrade to occur without a corresponding rate increase. In support of its proposal to do so, the Division cited the benefits of employing the newer telecommunication technology.

USWC testified that it is improper, and in the long run unwise, to increase capital expenditures just to keep rate base from declining when current depreciation expense exceeds planned construction expenditures. It is USWC's position that accelerated replacement of switches may be premature. According to USWC, such replacement should be undertaken when economic analysis demonstrates that the benefits of such a program exceed its costs. The Division has not conducted an economic analysis, and there is no evidence that its proposal is even technically feasible.

The technological upgrade of older central offices is an ongoing process. The rapid employment of new technology is not always advantageous. Lacking firm economic analysis we are unable to assess the benefits claimed for accelerated replacement of switches. At our request, the Division did, however, complete an examination of USWC's investment decisionmaking process, finding the process on all counts acceptable, according to testimony presented in this docket. While it is reasonable to expect that the objectives framing a company analysis of investment in new plant would not be the same as those we would employ to examine it, we can take comfort both in the Division's review and in the testimony on the record to the effect that most new services can be supplied with the older central office switches.

The Commission finds that an aggressive replacement program, at this time, is not justified on the record in this docket.

4. INDUSTRY AND INTER-GOVERNMENTAL TASK FORCE FOR E 9-1-1 IMPLEMENTATION

Upgrading USWC central offices to Enhanced 9-1-1 capability will have an effect upon independent telephone companies in the state, the extent of which is not known to this Commission at this time. Moreover, questions about funding the service throughout the state remain. Examples include whether Enhanced 9-1-1 subscriber surcharges can be pooled and whether Commission directives to the Company to establish the service carry weight with local governments which have legislative authority to tax to generate revenues to support it. We are, of course, concerned that financial feasibility may constrain service provisions in some Utah counties. The Division testified that it has not undertaken any detailed technical or financial discussions with either local governmental entities or independent telephone companies concerning these subjects. We find that a task force will have the advantage of bringing diverse, interested entities together to discuss common concerns. Out of this may come coordination and, as well, the information we seek. Therefore, we find that an industry/government task force is in the public interest and should be established, and direct the Division to chair and select the task force. Invitations should be tendered to the Committee, USWC, Contel, the ECU, the Utah Association of Cities and Towns and the Utah Association of Counties. The Division should provide a preliminary report to the Commission by March 1990.

ADDENDUM G

EXCERPTS FROM THE REPORT AND ORDER
OF THE UTAH PUBLIC SERVICE COMMISSION

JANUARY 25, 1988

DOCKET NO. 86-049-17

7.4
JAN 29 1988

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Petition)
of THE MOUNTAIN STATES TELE-)
PHONE AND TELEGRAPH COMPANY)
for Exemption from Regulation)
of Various Central Office)
Based Services.)

CASE NO. 86-049-17

REPORT AND ORDER

ISSUED: January 25, 1988

SYNOPSIS

By this Order, the Commission removes rate restrictions on Speed Calling, Call Waiting for multi-line business customers, Three-way Calling for multi-line business customers, and Toll Restriction services for multi-line business customers; allows Centron service to continue on a detariffed basis subject to certain conditions; directs Bell to submit a proposed tariff for network access registers and banded rate tariffs for Remote Call Forwarding and Call Waiting, Call Forwarding, Three-way Calling and Toll Restriction service for single-line business and all residence customers; and orders Bell and the Division to file a report on alternative approaches to tariff regulation of 976 Network Service within 95 days of this Order.

Appearances:

Ted D. Smith	For	The Mountain States Telephone and Telegraph Company
Brian W. Burnett, Assistant Attorney General	"	Division of Public Utilities, Department of Business Regulation, State of Utah
Sandy Mooy, Assistant Attorney General	"	Committee of Consumer Services
William Eagles	"	AT&T Communications

between a maximum and a minimum. We can find nothing in the statutes that requires that the tariffs of regulated utilities be set at one fixed rate. We therefore conclude that the Commission does have the power, if it finds that it is in the public interest, to establish tariff rates that are based on a maximum and a minimum price, such that the regulated utility has flexibility to price the service at price levels in between those parameters.

FINDINGS OF FACT

1. The primary competitors of Mountain Bell's Custom Calling services are the providers of terminal telephone equipment. The Commission finds that there are numerous such suppliers throughout the state of Utah. The Commission further finds that customers throughout the state can avail themselves of the opportunity to purchase terminal telephone equipment whether they are business or residence customers or whether they live in large cities or in rural areas.

2. Mountain Bell currently offers four basic Custom Calling features: Call Forwarding, Three-way Calling, Speed Calling and Call Waiting. Each feature allows telephone customers additional capabilities on their telephone service beyond that which is provided as part of basic service. Each of these features is provided by the central office switches of Mountain Bell.

3. Call Forwarding enables a customer to transfer incoming calls to another telephone number by dialing in a code, plus the telephone number to which the calls are being forwarded.

4. Three-way Calling enables a customer to add a third

customer to an on-going local or long-distance call without operator assistance.

5. Speed Calling enables a customer to call a pre-selected group of telephone numbers by dialing one or two digits rather than manually dialing the entire number of the called party.

6. Call Waiting gives customers the capability of receiving incoming calls, even though already engaged in a conversation with another party. When the customer is using the telephone, a tone signals him that another call is waiting to be answered. The incoming caller hears only a regular ringing signal. By flashing the switch hook, the customer with Call Waiting can place the initial caller on hold while answering the second call.

7. The Commission finds, based on all the evidence before it, that there are numerous varieties of terminal telephone equipment on the market that provide speed dialing capability. Such equipment is readily available to all classes of customers served by Mountain Bell. In Utah, Speed Calling is subject to effective competition; customers desiring services like Speed Calling have reasonable alternatives that are readily available to them; no provider of such services serves a captive customer base; and the detariffing of the rate levels for Mountain Bell's Speed Calling service for all classes of customers is in the public interest.

8. With regard to multi-line business customers, the Commission finds that there are numerous varieties of terminal

telephone equipment that provide readily available alternatives to Mountain Bell's Call Forwarding, Call Waiting, and Three-way Calling features. Therefore, the facts demonstrate that Call Forwarding, Call Waiting, and Three-way Calling are subject to effective competition in the market serving multi-line business customers; that multi-line business customers desiring such services have reasonable alternatives to the services provided by Mountain Bell that are readily available to them; that no provider of such services to multi-line customers serves a captive customer base; and that it is in the public interest to detariff rate levels for Mountain Bell's Call Waiting, Call Forwarding, and Three-way Calling services for multi-line business customers.

9. The Commission finds that with regard to single line business and all residence customers, that Mountain Bell has not adequately demonstrated that reasonable alternatives are currently available in the marketplace for Call Waiting, Call Forwarding, and Three-Way Calling services. We therefore find that in the residence and single-line business market it would not be appropriate to completely exempt such services from price regulation. However, the Division has proposed that Mountain Bell be given pricing flexibility in the form of a tariff that sets the upper rate for these services at the current tariff rate and which establishes the lower price limit at Mountain Bell's incremental cost of providing the service plus a 10 percent contribution. We find that such an approach is fair and reasonable and in the public interest, particularly in light of the fact that these services are non-essential, convenience services, the lack of

which does not materially impact the basic service provided to end users. We believe it is appropriate that Mountain Bell be given the flexibility to increase or maintain the number of customers obtaining such services so that it can maximize its revenues from such services, all of which will help to hold down rates for other services.

10. Mountain Bell provides three types of toll restriction services: Toll Restriction, Toll Diversion, and Individual Line Service (Selective Class of Call Screening). All three are methods by which customers can prevent users of their telephone sets from making long-distance calls. With Toll Restriction, when the user attempts to dial a long-distance call, the call is routed to a pre-recorded announcement. With Toll Diversion, a service available only to PBX or CENTRON customers, when the caller attempts to dial a long-distance telephone call, the call is diverted to a system attendant. With Individual Line Service, outgoing long-distance calls are limited to collect, third-party billing and calling card calls only.

11. The primary competitors to the toll restriction services are the providers of terminal telephone equipment. Such equipment provides the capability to prevent long-distance calls from being made. We find that such equipment is available to customers throughout the state of Utah. With regard to multi-line business customers, we find that such terminal equipment provides ready alternatives to the toll restriction services offered by Mountain Bell. The facts, therefore, demonstrate that in the state of Utah, toll restriction services are subject to effective

ADDENDUM H

EXCERPTS FROM THE REPORT AND ORDER
OF THE UTAH PUBLIC SERVICE COMMISSION

DECEMBER 31, 1985

DOCKET NO. 85-049-02

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Application)
of the MOUNTAIN STATES TELEPHONE)
AND TELEGRAPH COMPANY for Ap-)
proval of an Increase in Rates)
and Associated Tariff Revisions.)

CASE NO. 85-040-02

REPORT AND ORDER

ISSUED: December 31, 1985

APPEARANCES:

Ted D. Smith David E. Salisbury	For	Mountain States Telephone and Telegraph Company
Michael Ginsberg Assistant Attorney General	"	Division of Public Utilities, Department of Business Regulation, State of Utah
Brian Burnett Assistant Attorney General	"	Committee of Consumer Services, Department of Business Regulation, State of Utah
Terry Kolp Bruce Able	"	Department of Defense, Federal Executive Agencies
Michael Smith Assistant Attorney General	"	Utah State University, University of Utah, Weber State College, Department of Administration Services
Gregory Williams Wendy Faber	"	Omega Corporation, Utah Telephone Management Assoc.

By the Commission:

The application of the Mountain States Telephone and Telegraph Company (Mountain Bell, Company or Applicant) was filed on March 8, 1985, seeking an order of this Commission authorizing it to place into effect tariffs, rates and charges which would produce additional revenues of \$48,461,000. Of that amount,

As a Commission we are faced with the threat that acceptance of the Division's proposed adjustment may result in retribution from the IRS. The Division argues that such threats have been used in the past with regard to the interest synchronization adjustment, but that such threats are no longer taken seriously. In fact, the Commission has adopted the Division's position on interest synchronization in this case. (See paragraph 14, below.) Still, uncertainty exists as to what the IRS may do in reference to the Company's past and future investment tax credits if we adopt the Division position. For that reason, the Commission will adopt a position similar to that proposed by Mr. Michael J. Majoros, Jr. in the recent state of Maryland Case No. 7351, placed on the record herein as Exhibit A29, to establish and recognize the amount of the intrastate portion of the unamortized tax credits on the transferred assets--in this case the figure proposed by the Division--and to make clear that we intend to provide for the return to the ratepayer of this amount, over a reasonable amortization period, if this Commission subsequently determines that this can be done without placing past or future Company tax benefits in jeopardy. We so find.

12. EQUAL ACCESS COSTS

Equal Access, which was ordered by the federal courts, was included in test-year costs. The Division recommended that these costs be removed from the case because they will be recovered from interexchange carriers and not general ratepayers. The Company agreed to the adjustment, a reduction in revenue requirement of \$1,975,000, after the Federal-State Joint Board

recommended that Equal Access be separated on the basis of access minutes of use. The Commission finds that the adjustment should be adopted.

13. CASH WORKING CAPITAL LEAD LAG

Lead-lag adjustments as proposed by the Division would exclude non-cash components, average cash balances and working funds. A similar adjustment was also proposed by the Committee and the FEA. The Commission finds that the Division's proposed adjustment of a \$1,041,000 reduction in revenue requirement should be adopted because it is consistent with prior Commission policy as set forth in Utah Power and Light Company Case No. 82-035-13.

14. INTEREST SYNCHRONIZATION

The Division proposed that additional interest be imputed for income tax computation purposes (interest synchronization) in an effort to attribute the overall cost of capital to the debt component of the Job Development Investment Credit (JDIC). This adjustment was also proposed by the Committee and the FEA. The Commission will accept the Division's proposal, a reduction in revenue requirement of \$1,320,000, because we find that imputing a tax deduction to hypothetical interest on JDIC-financed ratebase is appropriate.

15. ANNUALIZATION OF WAGE INCREASE

The Committee and the FEA proposed an adjustment removing the annualization of 1985 wage increases. The Committee proposed, as an alternative, to annualize the year-end employee levels. The Commission discussed the annualization issue under